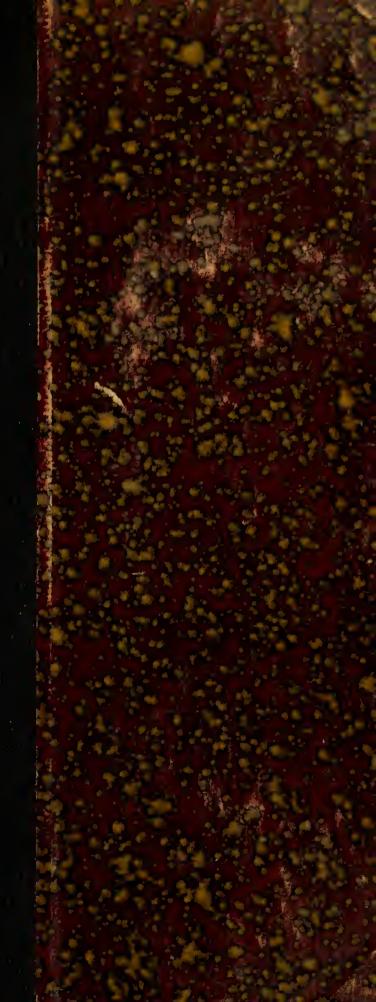
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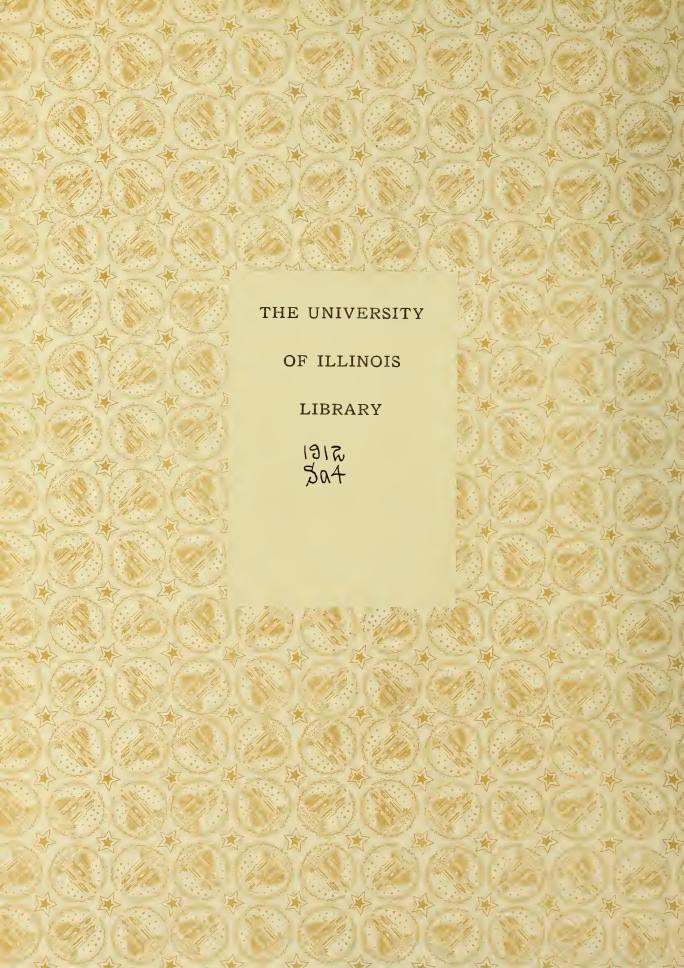
The Historical Evolution of
the Principle of Liability in the
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Economics

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# THE HISTORICAL EVOLUTION OF THE PRINCIPLE OF LIABILITY IN THE ILLINOIS CORPORATION

BY

## THOMAS WALTER SAMUELS

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#### THESIS

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I HEREBY RECOMMEND THAT THE THESIS PREPARED UNDER MY SUPERVISION BY

Thomas Walter Samuels

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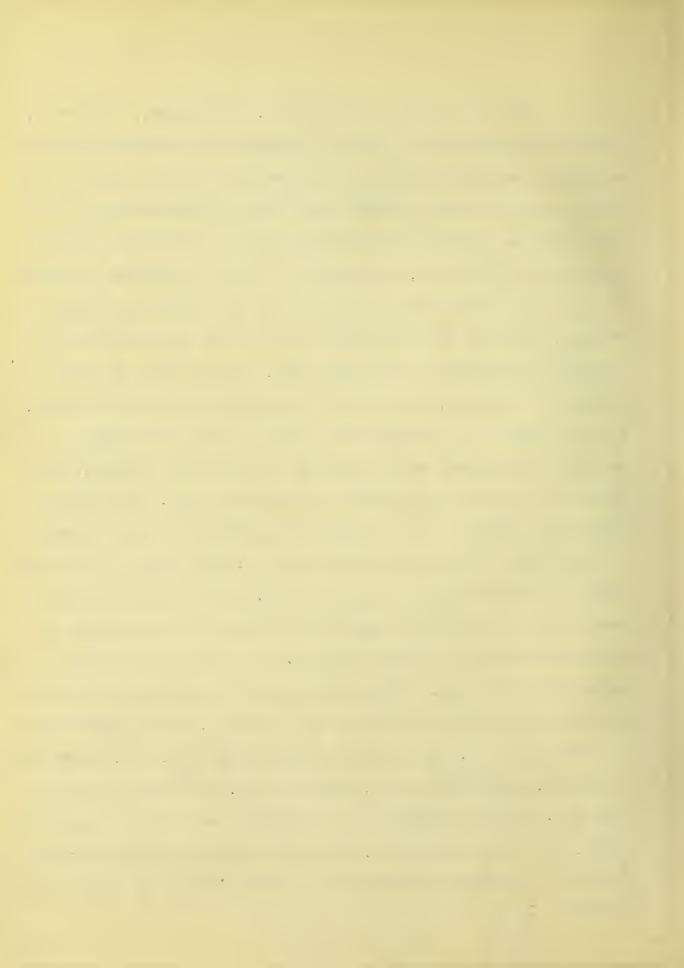
THE HISTORICAL EVOLUTION OF THE PRINCIPLE OF LIABILITY IN THE ILLINOIS CORPORATION.

One of the chief characteristics of the corporation of to-day is that liability for debts due to creditors is placed upon the business enterprise which the corporation carries on. The individual stockholders composing the modern corporation are not personally responsible for the debts of the company. If the company fails, they lose only the amount of their investment in the concern. This is so on the theory that they have paid for their stock in full: if they have not paid in full for their stock, they are, generally speaking, liable for the unpaid balance. In other words their liability for debts of the corporation is limited - limited to the amount they themselves owe the corporation. It is the purpose of this thesis to trace the historical evolution of the principle of liability in the Illinois corporation and to ascertain its present legal status. A rapid survey of the corporation itself, by way of preface, may not be wholly without profit.

The Romans were the first to develop the corporation to any important extent. They, however, only partially recognized the principle of limited liability. The corporation did not assume much importance until the 15th and 16th centuries in England, and even then limitation of liability was provided for in but few cases. Corporations developed very slowly, there being a very limited number in the United States until after the opening of the nineteenth century.

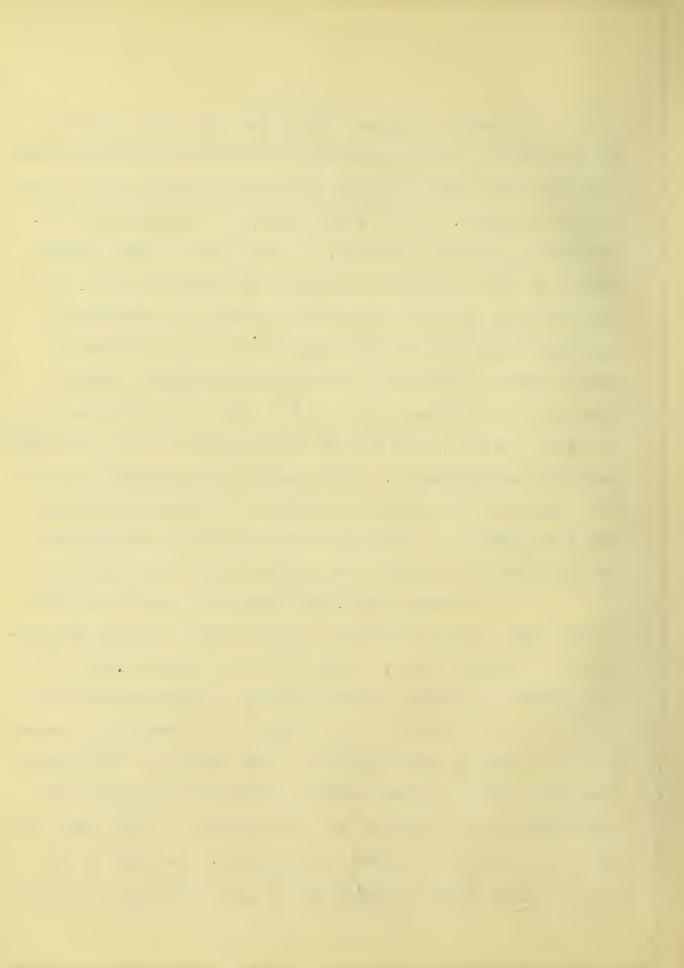
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With the advent of railroads, telegraphs, telephones, etc, the corporation as a form of business organization began to be adopted generally, until at the present time the bulk of our business is conducted through this form of organization. quote from an article by Professor Maurice H. Robinson of the University of Illinois, contributed to the Yale Review: "Formerly nearly all manufacturing was done by the individual entrepreneur, later by the partnership, now by the corporation; of the total production in the year 1900, nearly eight thousand millions in dollars, or almost 60 per cent of the total output, was the work of the corporation. Out of over five hundred thousand independent establishments in the United States, forty thousand in round numbers were in corporate form. The corporations were 12 per cent in numbers and produced 59.5 per cent of the output. The partnerships were 18.9 per cent of the total number of establishments, producing 19.7 per cent of the total Individuals owned 78.8 per cent of the number of production. establishments and produced only 20.6 per cent of the total amount of production. In certain lines the progress of the corporation has been particularly rapid, namely, in the manufacture of iron and steel, agricultural implements, coke, gas, electrical apparatus, manufactured ice, rubber goods, photographic goods, etc. etc. Thus concentration is accomplished through the corporation, and today, in a word, the corporation problem has to all intents and purposes superseded the trust problem of the previous decade."



A number of causes account for this rapid growth of the corporation. It is because the corporation possesses marked advantages over other forms of business organization that it has become so popular. In the first place, the corporation is endowed with perpetual existence. In fact, this is the leading feature of the corporation as defined by Blackstone; viz, "the corporation is an artificial person created for preserving in perpetual succession certain rights which being conferred on natural persons would fail in the process of time." When a stockholder in a corporation dies his share is transferred to his heirs, or sold, thus leaving the business and all its rights unchanged and unimpaired. When a member of a partnership dies, that partnership is thereby dissolved. The corporation being much more stable, is a far more desirable form of organization; and this fact has doubtless contributed much to its popularity.

In the second place, the snares in a corporation are divided into various amounts so that the small investor may purchase at least one share. The individual proprietor must sell his property as a whole; and the partner is limited in selling his part of the business by the necessity of securing the consent of his partners in the enterprise. This division of the capital stock into shares of small amounts gives the corporation the advantage of great flexibility in the number of those interested and in the amount of capital it may employ. The laws of the various states permit corporations to have any number of stock-



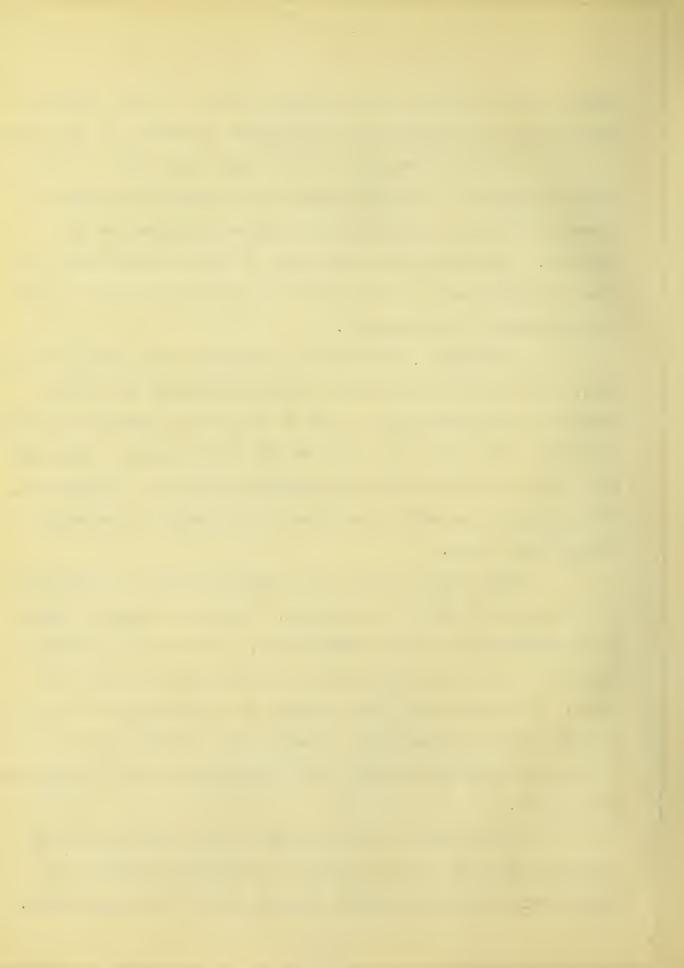
holders, even as few as three in many states. It can therefore obtain a small or large amount of capital according to its needs.

A further advantage of the corporation lies in its central management. Usually there is a president and board of directors to whom is entrusted the active management of the business. The individual shareholder is thus relieved from active participation in the business as in the case of the single proprietorship or partnership.

And finally, the modern corporation recognizing, as it does, the principle of limited liability by which the stock-holder is responsible only to the amount of his investment in the enterprise, and not to the full extent of his private resources as in the case of an individual proprietorship or a partnership, has furnished a powerful incentive to all classes to save and invest their money.

These then are the chief characteristics and advantages of the corporate form of enterprise. And while they are common to all corporations of the present day, it must not be thought that all of them have distinguished the corporation from the first. As stated above, the adoption of the principle of limited liability is comparatively recent. Not until the latter half of the nineteenth century was this principle generally recognized and adopted.

Before Illinois was admitted to the Union as a state and until after the middle of the century practically all companies were incorporated under special acts of the legislature.



Some of these acts contain provisions covering liability for debts and some are silent on that subject. It is quite characteristic of the earliest acts to hold the president and board of directors liable in their private capacities for debts of the company. For instance we find this provision in an act passed in 1817 by the Territorial Assembly to incorporate the Little Wabash Navigation Company: "When anything is due to any person or persons from said company, and the same shall remain unpaid for thirty days, it shall be lawful for any court in the county having jurisdiction of like sums, to give judgment for the amount of the sum due against the president and directors of said company, with interest from the end of the said thirty days, to the time of payment, and costs."

"And the same summary remedy is hereby given against all persons who shall or may be bound by bond, bill, obligatory, or note in writing, or assessment of the same to the president and directors of the Little Wabash Navigation Company."

It will be noticed that no limit whatever is placed upon the liability thus imposed upon the president and directors. When "anything is due to any person" from the company the president and board of directors are responsible for its payment. It would seem that the fixing of such heavy, personal liability upon the officers of the company would cause them to be very careful in incurring debts or obligations. The second clause is quite consonant with the first, and is doubtless intended to reach subscribers to the capital stock of the company as well as other



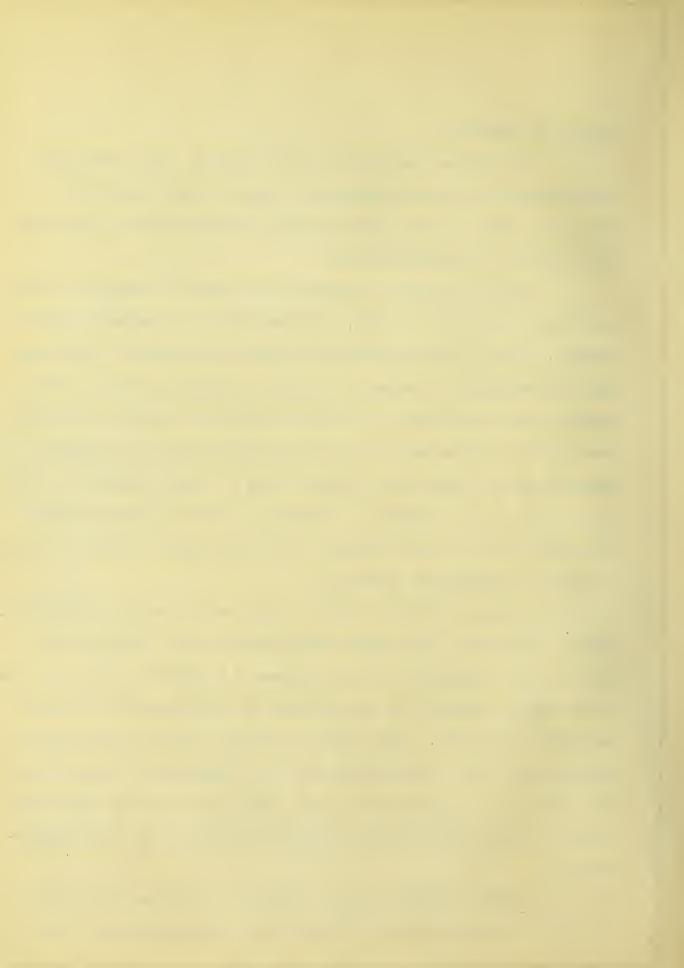
classes of dobtors.

In another act of this early period, the president and directors are held responsible only for debts exceeding twice the amount of the capital stock; but nothing is said about the liability of stockholders.

The first act to recognize in anyway a limitation upon liability was passed in 1821, incorporating the Sangamon Milling Company. Here it is expressly provided that nothing in the act shall be construed to exempt the private property of the stock-holders from the payment of "such a portion of each or any debt that may be contracted by said company whilst they are stock-holders, as the stock such stockholders may own will bear to the whole stock of the company." Nothing is said in the act about the amount of the stock required to be paid up. We may call this a case of proportional liability.

During 1823 and 1824 not many companies were organized. The few, however, which were incorporated placed little or no limit on the liability of stockholders. In 1824 is found for the first time a general act authorizing the incorporation of manufacturing companies. Here again we find a case of proportional limitation: "Each stockholder shall be personally and individually liable for the payment of all debts which may be contracted by such company in proportion to the stock held by them respectively."

From this time on all companies organized under this l. Act to incorporate the Illinois Navigating Company, 1818.



general act have of course the same liability provisions. A great many charters of companies not formed under this act for the next ten years place practically no limitation whatever on the liability of their stockholders. The act for the incorporation of Franklin College (1827) provides that the trustees and members of the corporation shall be liable in their private capacities for all contracts made.

Most of the laws passed by the General Assembly in 1834 and 1835 for all companies except railroads, insurance, and banking companies (which will be treated in separate sections) make no provision whatever for liability to creditors; one, however, provides that the stockholders shall be liable to the amount of their unpaid stock. The act incorporating the Mount Carbon coal Company (1835) contains this provision: "Each and every stockholder shall be, in his individual capacity, liable for the debts and performance of all contracts entered into by said corporation, to the amount of the balance unpaid on the stock of such stockholders."

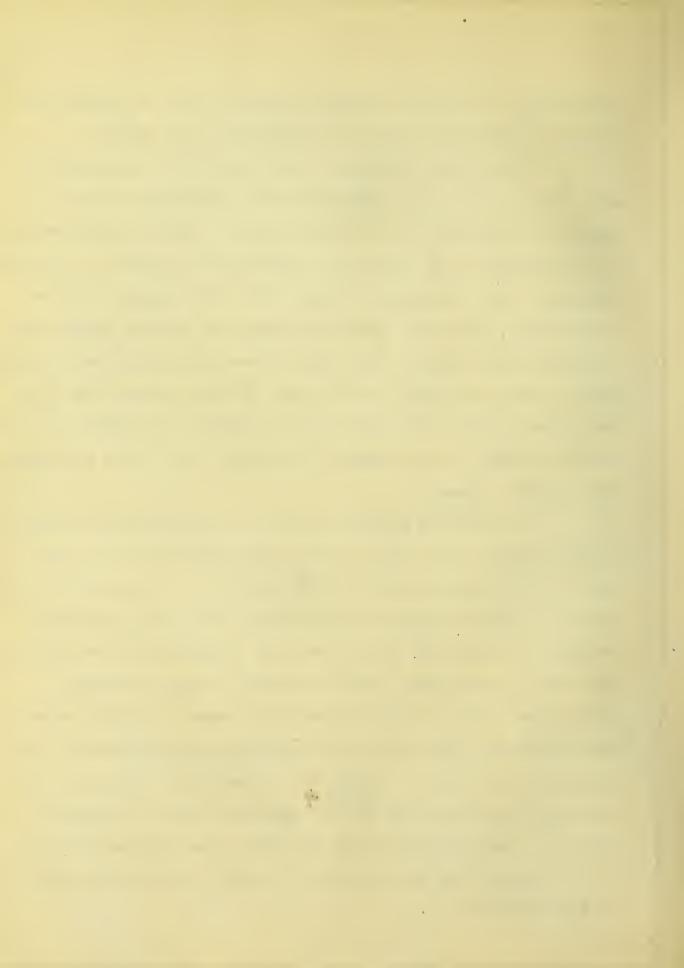
The striking thing about the incorporation laws of this whole period is the lack of uniformity with reference to the liability of stockholders. In some acts, stockholders are limited in their liability; in others passed at the same session of the legislature, they are made individually responsible for debts to the full extent of their private property; while still others make no provisions at all for the payment of debts. In

other words, the General Assembly seemed to have no established policy or settled principles for regulating this matter.

In the late thirties a good many of the incorporation acts contain provisions prohibiting the incurring of debts in excess of the amount of the capital stock. The following section in the charter of the Monticello Manufacturing Company is typical: "Provided, that the amount of debts which the company shall at any time owe, shall not exceed the amount of capital stock, and in case of such excess, those under whose administration it shall happen, shall be holden for the same, in their natural and private capacity; but this shall not be construed to exempt the corporate property of the company, from being also liable and chargeable for such excess."

In 1818 the corporation was not of sufficient importance in Illinois to find a place in the state constitution of that year. In the constitution of 1847, however, a whole article is devoted to the subject of corporations. It is here provided, Article X, section 11, that "dues from corporations, not possessing banking provileges, shall be secured by such individual liabilities of the corporators or other means as may lie prescribed by law. That this clause by implication reserves to the legislature the right to change or increase the liability of a upheld of stockholder was subsequently the Appellate Court in Parkhurst

Mexican S. E. R. Company, 102 Ill. 507. The section relative to the liability of stockholders in banking institutions will be discussed further on.



In 1847 the General Assembly provided for the formation by general act of limited partnerships. The act provides that limited partnerships may be formed consisting of one or more persons who are to be called general partners, and who are to be jointly and severally responsible as general partners were then; and, in addition, one or more persons who shall contribute a specific amount of capital in cash or other property, at cash value, to the common stock. These latter were to be known as special partners, and were not to be liable for the debts of the partnership beyond the amount contributed by them, respectively, to the capital stock.

ment in the state for general incorporating acts. Corporations were growing in great numbers, and as a result of this rapid growth every session of the legislature found itself literally besieged with petitions for special charters. Altogether too much time of the General Assembly was taken up with the consideration of these special acts. Besides, it was felt by many that only those corporations with influential backing could get an adequate hearing before the legislature, and that consequently the industrial development of the state was being retarded. In response, therefore, to this growing sentiment, general acts were passed by the General Assembly of 1849 authorizing the formation of corporations for manufacturing, mining, and mechanical purposes, for the formation of railroad companies, institutions of learning, and for the construction of plank roads, and the es-

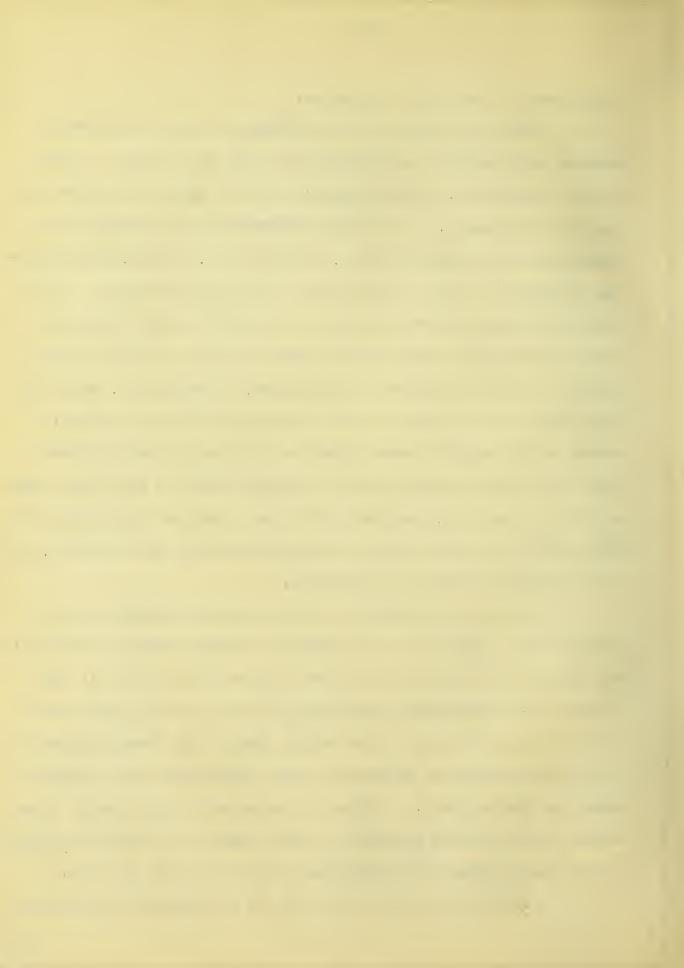


tablishment of telegraph companies.

becomes more definite and conscious of its own purpose. There is more uniformity. These general acts are especially interesting in this respect. In the act authorizing the formation of corporations for manufacturing, agricultural, mining, and mechanical purposes we find the following liability provisions: "All the stockholders of every company incorporated under this act shall be severally individually liable to the creditors of the company, in which they are stockholders, to an amount, equal to the amount of stock held by them respectively until the whole amount of the capital stock fixed and limited by such company shall have been paid in; and the capital stock so fixed and limited shall be paid in, one half within one year and the other one-half within two years from the incorporation of said company, or such corporation shall be dissolved."

Here is an attempt to keep the assets equal to the liabilities. Since the full amount of capital stock is evidently not going to be paid in all at once, special provision is made to hold the subscribers individually liable for all debts until it is fully paid in; in other words, during the formation period of the corporation an unusually heavy responsibility is placed upon the stockholders. Instead of being held liable only to the extent of the unpaid portion of their stock, they are held liable to the whole extent of their stock until it is all paid in.

Further on in the same act is the following provision:



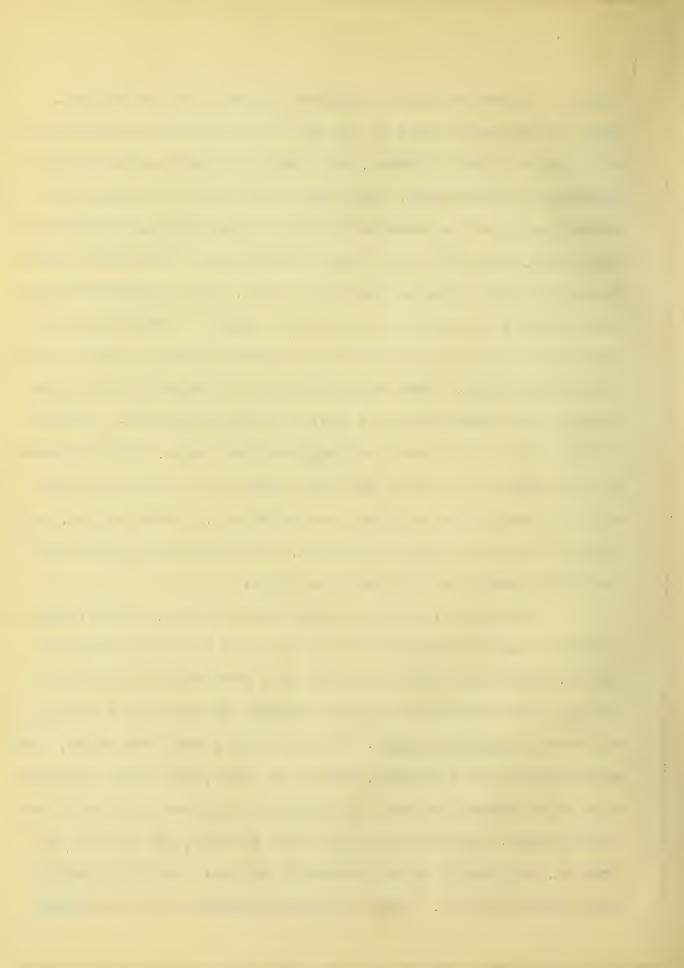
"Executors, guradians, and persons holding stock as collateral security are not personally liable on stock held as such; but the persons pledging such stock shall be considered as holding the same, and shall be liable accordingly, and the estate and funds in the hands of such executors, administrators, guardians, or trustees, shall be liable in like manner and to the same extent as the testator, or intestate, or the ward or person interested in such trust fund would have been, if he had been living and competent to act, and held the stock in his own name."

This is the first reference found in any Illinois corporation act fixing the status of persons holding fiduciary relations when dealing in stocks. It was held, however, in Shurwood v. Illinois Trust and Savings Bank, 195 Illinois. 112, that one who desires to claim the benefit of the exemption provided by the statute for trustees, administrators, executors, and other persons holding fiduciary relations, when dealing with stocks of corporations within the state, should protect himself and the creditors of such corporations alike, by causing his representative character and the identity of the true owner to appear upon the records of the corporation, for a creditor of an insolvent corporation may hold those liable who appear to be the legal owner of the stock, even though transfers have been made which do not show upon the books. In 129, Illinois. 64, the evidence developed the fact that after a part of the capital stock of a corporation had been subscribed, and for the purpose of organizing the corporation, one of the subscribers was induced by the



others to subscribe for the balance of the stock as trustee, under the agreement that he was not to be assessed on such shares or to become liable thereon, but that all should assist him in disposing of such stock. The court held that as between such stockholders and the creditors of the company he was liable for such stock, but not to the other stockholders. The fact that he placed the word "trustee" after his name, made no difference in his liability to creditors. Said the court: "Creditors are entitled to look to the stock as it appears upon the face of the subscription list. Each stockholder has a vested right in the contract for subscription of every other stockholder." Clark, in his authoritative work on "Corporations" says, "If he appears on the books as the legal and real owner, he is as far as the rights of corporate creditors are concerned, a stockholder, and subject to the statutory liability, though he may in fact hold the stock merely as collateral security."

In Howe v. Illinois Agricultural Works, 46 Ill. App. 85, we have a case slightly different from the one just discussed. One Dr. Mendenhall took the stock of a corporation as paid up, and as a mere depository for the company which was the known and avowed cestuique trust. "His holding", said the court, "was merely that of the company, and as we think, the fair, equitable view is to regard the stock remaining in his hands as still unissued stock. He did not take it for himself, nor did he intend to, nor was it so understood by anyone. We freely admit," continues the court, "that no man can subscribe for corporate



stock, known to be subject, and escape liability by appending the work "trustee" after his name. It would be absurd to allow anyone to do this, and cast votes and claim dividends, on such stock and then escape responsibility by insisting that he acted on behalf of some undisclosed person." The court held that Dr. Mendenhall's case was of an entirely different nature, since the company was the known and avowed cestui que trust.

Illinois has not kept pace, industrially speaking, with the older eastern states. As early as the twenties New York made her stockholders liable for debts due to laborers and apprentices for services performed. It was not, however, until 1849 that Illinois took up a progressive position with reference to the treatment accorded her industrial workers. In the general act of this year, stockholders, for the first time in the history of the state, are made jointly, severally, and individually liable for all debts due and owing to their laborers, servants, and apprentices, for services preformed for the corporation. This is a most reasonable and desirable provision and it is to be regretted that our state delayed so long in adopting it.

The same act in question provided further that no stockholder should be held personally liable for the payment of any debt contracted by any company formed under its provisions, which was not paid within one year from the time the debt became due, unless a suit for the collection of such debt was brought against the company within one year after the debt became due; and it was further provided that no suit might be brought against

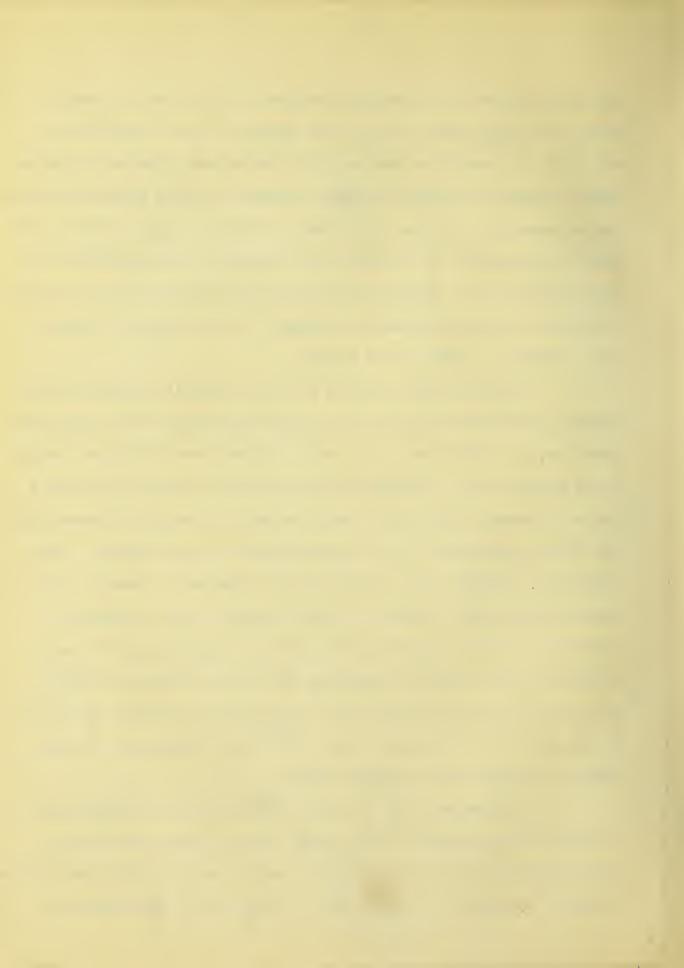


any stockholder in the company, unless the suit was commenced within two years from the time he ceased to be a stockholder, nor until an execution against the company was returned unsatisfied in whole or in part. With reference to this latter provision the supreme court of the state held (Tarbel v. Page, 24 Ill. 46) that the necessity of bringing suit against the corporation before enforcing the personal liability of the stockholders is not obviated by the fact that the company is insolvent and that a suit against it would be of no use.

Evidently the purpose of this liability clause was to protect stockholders from being proceeded against for debts long past due, and furthermore to protect them after they have ceased to be stockholders. Without this provision the creditors of a bankrupt company might have recourse against solvent persons who had long since ceased to be stockholders in the company. This provision, however, was doubtless not intended to protect the shareholder alone, but the creditor as well, for it makes it impossible for the shareholder to avoid liability by the mere transfer of his stock. Creditors are further protected by a provision in the act which holds the trustees personally and individually liable whenever they shall the indebtedness of the company to exceed the capital stock.

The general act of 1849 authorizing the construction of plank roads furnishes our first case of double liability.

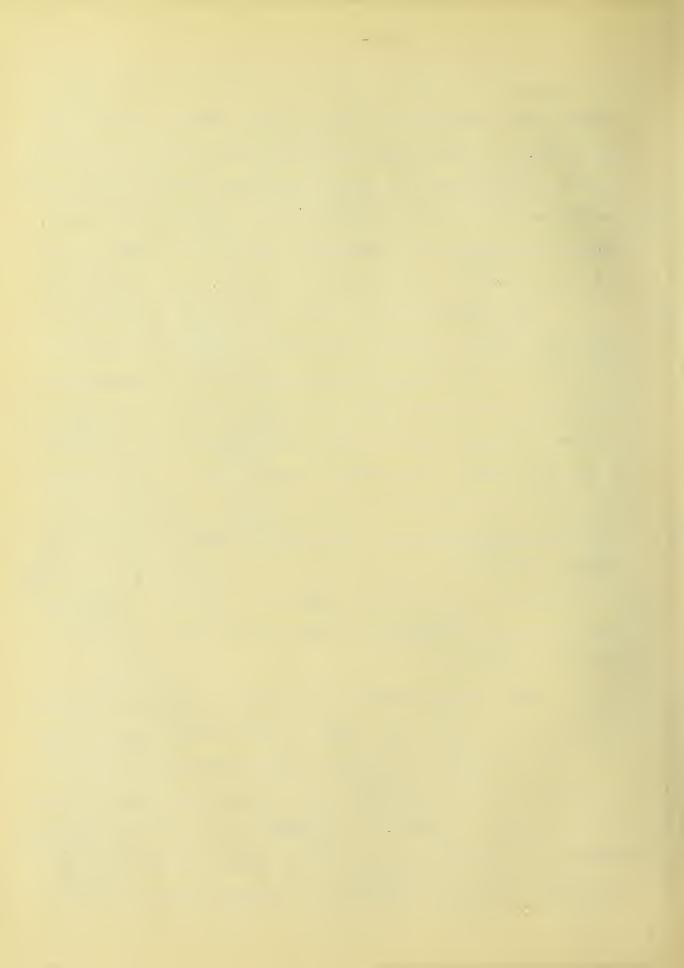
The stockholders of every company, reads the act, shall be liable in their individual capacity for the payment of the debts of



such company for an amount equal to the amount of stock they severally have subscribed or hold in the company over and above such stock, to be recovered of the stockholder who is such when the debt is contracted, or of any subsequent stockholder; and any stockholder who may have paid any demand against such company, either voluntarily or by compulsion, shall have a right to resort to the rest of the stockholders liable, for contribution.

The purpose of this heavy liability is evidently to insure the creditor against any hazard. It is not unusual to find double liability imposed upon shareholders in banking institutions at the present time, but such stringent liability in the case of stockholders in plank road companies in the middle of the last century was certainly unusual and a little surprising. It is significant of a spirit of equity that the stockholders who have met their obligations to creditors are given recourse against those who have not. The act also provides that the dissolution of any company shall not release or affect the liability of any stockholder, which may have been icurred before such dissolution.

The act also enjoins all companies organized under its provisions not to let their debts or liabilities exceed 50 per cent of the amount of its capital stock actually paid in; and in case such debts or liabilities do at any time exceed 50 per cent of the paid up stock, the stockholders are held jointly and severally individually liable for the excess, in addition to their other individual liability as provided for in the act.

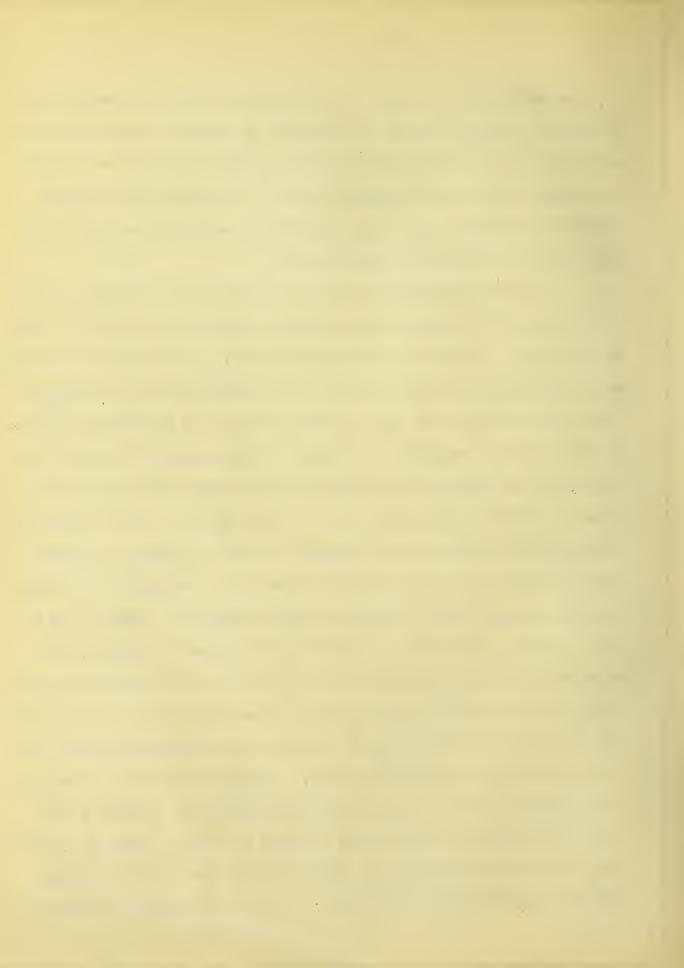


Not only is thore a growing tendency during this period to be more careful and definite with respect to the rights and obligations of persons concerned in corporations, but there is also a noticeable attempt to indicate in detail the method to follow in collecting sums due. For instance, in the act under discussion occurs the following detailed section which is quoted verbatim in to show the exceeding cautiousness of the charter: "In any action against any company formed under the provisions of this act, the plaintiff may include as defendants any one or more of the stockholders of such company, who shall, by virtue of the provisions of this act, be claimed to be liable to contribute to the payment of the plaintiff's claim, and if judgment be given against such company, in favor of the plaintiff, for his claim, or any part thereof, and one or more stockholders so made defendants shall be found to liable as aforesaid, judgment shall be given against him or them and shall show the extent of his or their liabilities individually. The execution upon such judgment shall direct the collection of the sum for which it may be issued, of the property of such company liable to be levied upon by virtue thereof; and in case such property sufficient to satisfy the same cannot be found, that the deficiency, or so much thereof as the stockholders who shall be defendants in such judgment shall be liable to payment, shall be collected of the property of such stockholders respectively, and if in any such action any one or more of such stockholders shall be found not to be liable for the demand of the plaintiff, or any part there-



of, judgment shall be given for the stockholders so found not to be liable, but no verdict or judgment in favor of any such stockholders shall prevent the plaintiff in such action from proceeding therein against the company alone, or against the company and such defendants who are stockholders as shall be liable for such demand, or some portion thereof."

The legislature of 1852 in amending the charter of the Illinois and the Mississippi Telegraph Company provided for what we might call a case of divided liability. The board of directors were authorized and empowered to divide their lines of telegraph into such divisions as they thought proper and convenient and to provide for the separate government and management of such divisions, and to separate the financial interests and liabilities of each division from the other. It was provided that any debt or liability contracted or incurred by the officers or governmental authority of one division, for or on the account of that division, should only create a special liability against the said company, so as only to subject the property, assets, resources and funds of such division to the payment thereof. Just what the intention of the law here is and how this separation of the lines into divisions each having its own government and its own liability is difficult to see. It would seem that a reasonable interpretation of the law would permit the directors to issue stock against the assets of each division. Such an arrangement would correspond to the large corporation of the present day with its subsidiary branches. There is no record in the



minutes of the House and the Senate journals throwing any light on the reasons for authorizing this particular company to separate its financial interests and liabilities. The reason for this arrangement is probably to be found in the nature of the telegraph business itself, being peculiarly adaptable, as it is, to subdivision. There is no record of the courts being called upon to interpret the liability provisions of this charter.

In an act to amend an act in aid of the Spoon River Navigation Company, approved June 23, 1852, the company is expressly prohibited from making any payment, assignment or transfer of the company's property to any one or more of its creditors, for the purpose of prefering one or more to the whole of their creditors, and any such payment, assignment or transfer is made null and void as against the other creditors. It would seem that a strict interpretation of this clause would prevent, not only the misuse of the company's property, but, to some extent, the juggling of stock.

Where preference to particular creditors is not expressly prohibited by statute, the case is different. Clark on Corporations says, "By the weight of authority, the rights and powers of a corporation in this respect are identical with those of animidvidual, and it may lawfully prefer particular creditors, unless prohibited by statute." In Glover v. Lee 140 Ill. 102, where a corporation after a loss by fire, at the instance of a bank holding its notes, with the assent of the insurance company, assigned certain policies of insurance to the bank as a further



security, before any other creditors acquired any lien or took any steps to reach the assets of the company, that the bank, by the assignment of the policies acquired the right to have its debt first paid out of the insurance money, as against subsequent attaching creditors. Said the Court, "When the Bank saw that its debt was in danger of being lost, on account of the destruction of the property of the corporation by fire, it had the undoubted right to obtain security for the debt from the Mattress Company, and the Mattress Company had the right to secure one creditor in preference to another, if it saw proper, and a transaction of this character, based upon a sufficient consideration and made in good faith, as was the case here, will be sustained." In 110 Ill. 316 the Supreme Court, quoting with approval Thompson on the Liability of Stockholders, said, "Where separate actions are tolerated, the creditor of the corporation first suing a stockholder in respect of his individual liability, acquires by the bringing of a suit, a preference over other creditors, which neither they nor the stockholder can defeat, unless possibly by bringing a general winding up bill. Such a suit may be said to be an equitable attachment of the stockholders' liability to the extent of the plaintiff creditor's claim. But," continues the court, still quoting, "it follows that the stockholder can not after notice of such a suit, defeat the suing creditor by paying the claim of other creditors as far as to exhaust his liability. If such a power existed, the stockholders could use it as a weapon to defeat creditors altogether.



In 1857 the legislature in fixing the liabilities of vessels made all steam-boats navigating the rivers within or bordering on the state liable for debts on account of such vessels by the master, owner, steward, consignee or agent for materials, supplies or labor in building, repairing, furnishing or equiping the same, or due for wharfage and also for damage arising out of any contract for the transportation of goods or persons, or for any injuries done to persons or property by such craft, or for any injury done by the captain or mate or any officer thereof, or by any person under the order or sanction of either of them to any person or hand on such boat at the time of the infliction of such damage or injury. And it is further provided that any one having ground for such demand may proceed against the owner or owners or the master of such craft, or against the craft itself. It would thus seem that persons holding stock in such a boat would be liable to an unlimited extent.

We see by this time that there is no uniformity as yet with respect to the liability of stockholders. Incorporation acts passed on the same day by the General Assembly reveal differences in this feature even where there is no vital difference in the nature of the businesses incorporated. Thus the same legislature which provided for the unlimited liability just cited also provided in an act to incorporate the Chicago Merchants Exchange Company that stockholders should be liable only for their unpaid stock, and not then, unless the creditor had first brought a suit against the corporation for the collection of his



debt within six years after the debt became due and an execution against the corporation had been returned unsatisfied in whole or in part.

During the period from 1859 to 1869 some of the acts made the stockholders liable to the amount of their unpaid stock, some to the amount of stock subscribed by them, and a great many mention no liability at all.

In 1867 in incorporating the Fox River Hydraulic and Manufacturing Company, the General Assembly after fixing the liability of stockholders to the amount remaining unpaid on the stock held by them, prohibits, without the concurrence of at least three-fourths in value of all the stockholders any assessment upon the paid up stock; and in no case may the assessment or assessments ever exceed twenty five dollars per share.

In 1869 we have one of the first cases of directors being permitted to issue stock for patent rights. The board of directors of the Northwestern Liquid Fuel Company was authorized to pay any sum not exceeding five hundred thousand dollars, in the stock of the company, at its par value for any and all such patent rights as the directors deemed necessary or expedient for the company to own, for the purpose of successfully carrying on the business of the company, which stock, so paid was not to be liable to any assessment by said company, nor were the holders of this stock to be individually liable for any indebtedness of the company.

<sup>1.</sup> This of course is not a case of bonus stock nor over-valuation, because patent rights may be just as valuable though not so tangible as material property.



In the incorporating act of the Belvidere Union Hall Association we find a clause which taken literally would certainly afford an excellent opportunity for avoiding liability by the transfer of stock just prior to the rendering of the judgment against the company. "No stockholder", says the act, in the corporation shall be held liable for the debts of the said corporation in any other amount than the stock by him held at the time of the rendition of judgment against said corporation."

Up to this time there were two or three general incorporation acts, but these being limited to certain kinds of business, were wholly inadequate to meet the thousands of corporate enterprises that were applying to the legislature for permission to carry on business in the state. Accordingly the General Assembly of 1872 passed a general law for the incorporation of practically all kinds of companies. The opening clause of the act will afford an idea of its nature:-

"Be it enacted, etc. That corporations may be formed in the manner provided by this act, for any lawful purpose except banking, insurance, real estate brokerage, the operation of railroads and the business of loaning money.

"Whenever any number of persons not less than three, nor more than seven, shall propose to form a corporation under this act, they shall make a statement to that effect under their hands and duly acknowledged before some officer in the manner provided for the acknowledgment of deeds, setting forth the name of the proposed corporation, the object for which it is to formed,

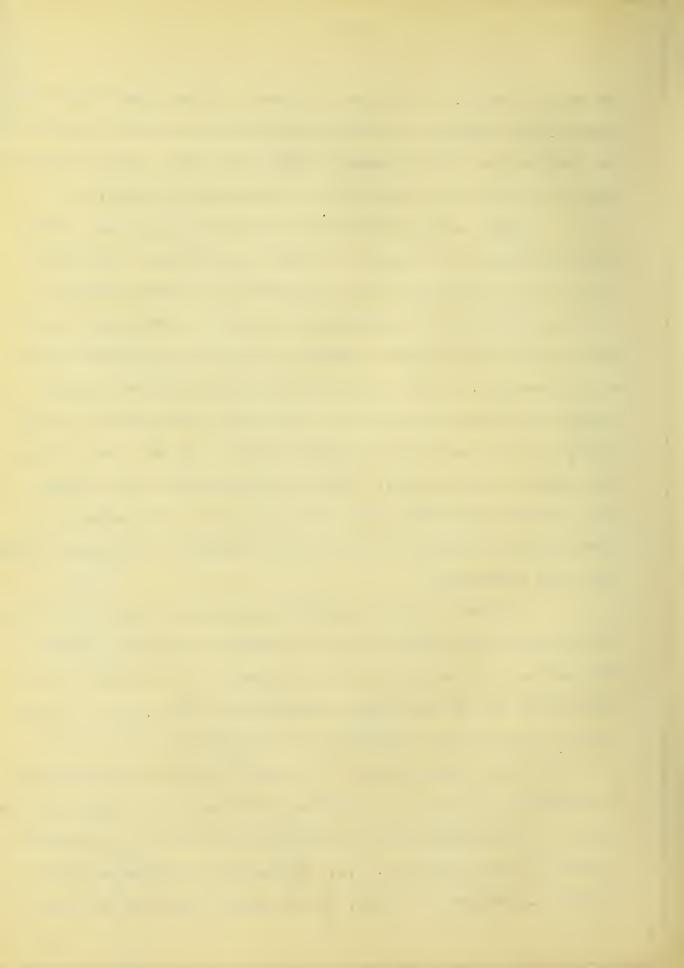


its capital stock, the number of shares of which such stock shall consist, the location of the principal office and the duration of the corporation, not to exceed ninety nine years, which statement shall be filed in the office of the Secretary of State."

These acts provide that stockholders shall be liable for debts only to the amount of their unpaid stock. This provision is in accordance with the generally accepted theory of the true nature of the corporation as being a personality separate and distinct from the natural persons who have contributed to its creation. If the corporation is a distinct entity it follows logically that those who have given their money to that entity thereby loose their responsibility to it as soon as they have paid in their money. They are responsible to the company only for the money which they have promised to the company but have not paid, that is, for the unpaid portion of the stock which they have subscribed.

Concerning this liability the Supreme Court in 154 Ill.

485 expressed the opinion that "The Capital stock of insolvent
Corporation is a trust fund for the payment of its debts. If a
stockholder has not paid his subscription in full, he is liable
for the debts of the corporation to the extent of the unpaid
portion of his subscription. It is the duty of the directors of
a corporation to manage its capital stock as a trust fund for the
benefit of its shareholders while it exists and of its creditors
in case of its disolution..... The unpaid stock is as much a
part of the corporate assets, as the money which has been paid



upon the stock. The obligations of a subscriber can not be released or surrendered to him by the trustees of the corporation, nor will stockholders be permitted to agree among themselves that their shares shall be taken at nominal value, or be non-assessable where such agreement operates to the injury of creditors." continuing, the court defines the status of an innocent purchaser of unpaid stock. Such an assignee of stock "does not become liable to the corporate creditors for the unpaid balance, where the stock has been issued as fully paid, and he has acquired the same in good faith and without notice that it has not been fully paid. But where a person purchasing stock issued as paid up has notice that it has not been paid, his liability is the same as the party who transferred it to him."

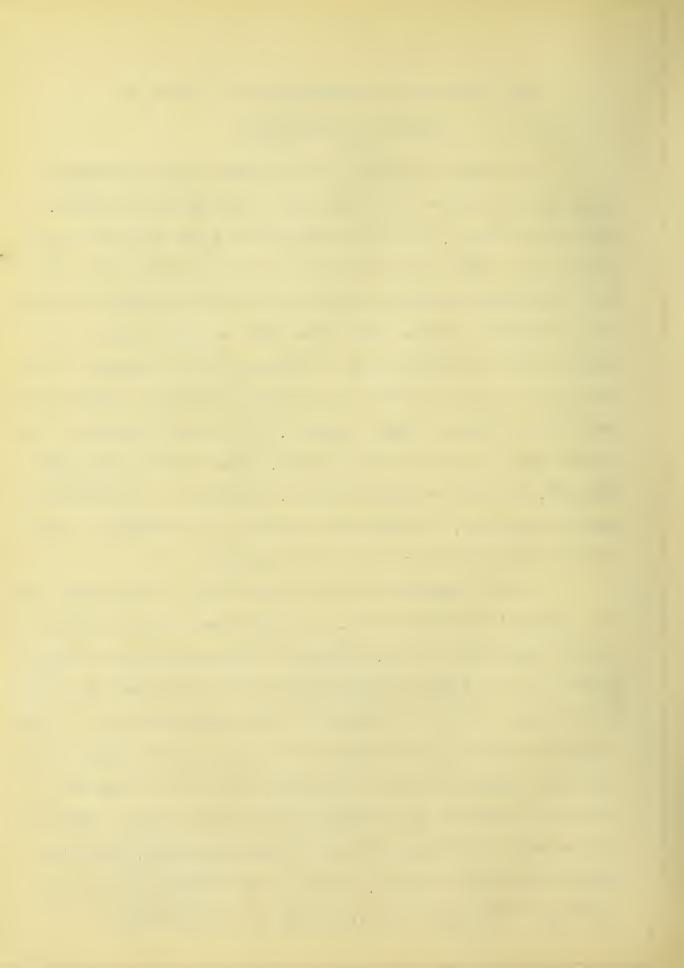
<sup>1.</sup> In Meints v. E. St. Louis co-operative Mill Company, 89, Ill. 48, the Supreme Court held that a stockholder in a corporation who owes for unpaid stock upon which a call has been made and notice given, may be garnished on a judgment recovered against the company. In 102 Ill. 196, the court held that a creditor of a corporation which has ceased to exist, and no judgment at law can be obtained against it, may maintain a bill in equity to enforce the unpaid subscription.



The Liability of Stockholders and Others in Railroad Corporations.

asked the legislature for a charter. This charter provided, among other things, that the subscription books should be open for one year before the passing of the incorporating act, and that five dollars should be paid on every share (fifty dollars). The act further provides that "the whole of the stock of the company and corporation shall be deemed personal property, and together with all the tools, implements, machinery, apparatus of every description used and employed, or on hand belonging to the company shall be liable to be seized, executed and sold, after judgment, to make good any contract, agreement, or stipulation made by any agent, or authorized person of the company." This is the only liability clause in the charter.

In an amendment to the Jacksonville and Meredosia Railroad Company's charter (1836), it is provided that in case a
company negotiates a loan, holders of stock shall never be required to pay a larger amount on the stock subscribed than will
be necessary to pay the interest on the amount borrowed, and the
principle when due, five dollars to be paid on each share at the
time of the subscription. The amount which the company may
borrow is limited to the amount of its capital stock. Thus it
will be seen that the creditors are doubly secured, having recourse against the tangible assets of the company, and in case
the assets have depreciated, against the stockholders.



A number of incorporation acts of this period provide that the shares of the company may be assessed to the extent of one hundred dollars a share, which, where the stock is required to be fully paid up, would amount to double liability.

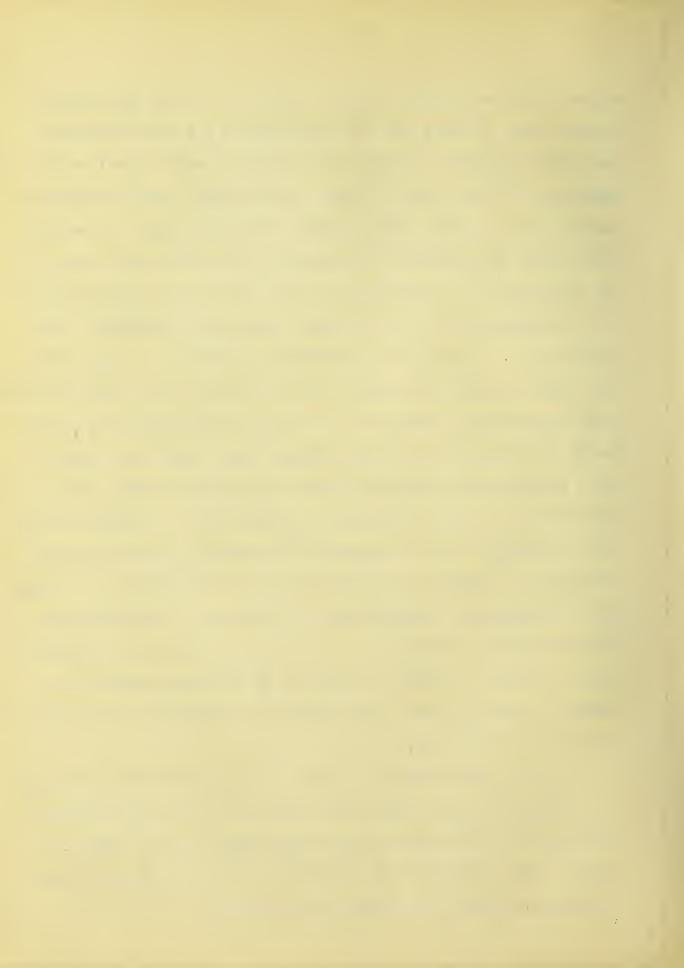
In the railroad companies incorporated during this time as well as general manufacturing companies, we find a great many cases of unlimited liability, and cases in which the liability of stockholders is limited in varying degrees. For instance the act by which the La Salle Dickson Railroad Company was incorporated (1841) provides that the individual property of the president, directors and stockholders shall be liable for all contracts or liabilities of the company to an amount proportionate to the amount of stock held by each of them respectively. Six years later the General Assembly made each stock holder in the Union County Charcoal Road Company liable in his private property, real and personal, to a sum equal to the amount of stock owned by him for all debts contracted by the company; and extended such liabilities for one year from the time he had parted with his stock. It will be noticed that the act makes each stockholder liable to the amount of stock owned by him and not merely to the amount unpaid on his stock. This point was brought out in Root v. Sinnock, 120 Ill. 350. The stockholders are liable as principle debtors, substantially as if they were partners except that the liability of each is limited to the amount of his stock.

In 1849 the same reasons which impelled the legislature to pass a general act for the incorporation of manufacturing,



agricultural and mining companies led them to pass the general railway act. In this act the stockholders are held severally individually liable to the creditors to an amount equal to the amount of the stock held by them respectively, for all debts or contracts made by the company until the whole amount of capital stock fixed and limited by the company shall have been paid in and certified to. Evidently it would here be to the advantage to the stockholders to pay up their stock and thus avoid liability on it. It was held in Diversey v. smith 103. Ill. 378, that where a statute provides that the trustees and incorporators shall be severally liable for all debts of the corporation till the whole capital stock of the company shall have been paid in and a certificate stating that fact filed and recorded, this liability was in the nature of a penalty and so an action to enforce it did not survive against the executor of the deceased stockholder. Authorities agree that where the liability imposed by a statute upon a stockholder for debts of a corporation is contractual and not penal, the cause of action does not abate upon his death, but survives and may be enforced against his personal representative. This point is sustained by the Illinois courts in 213 Ill. 178.

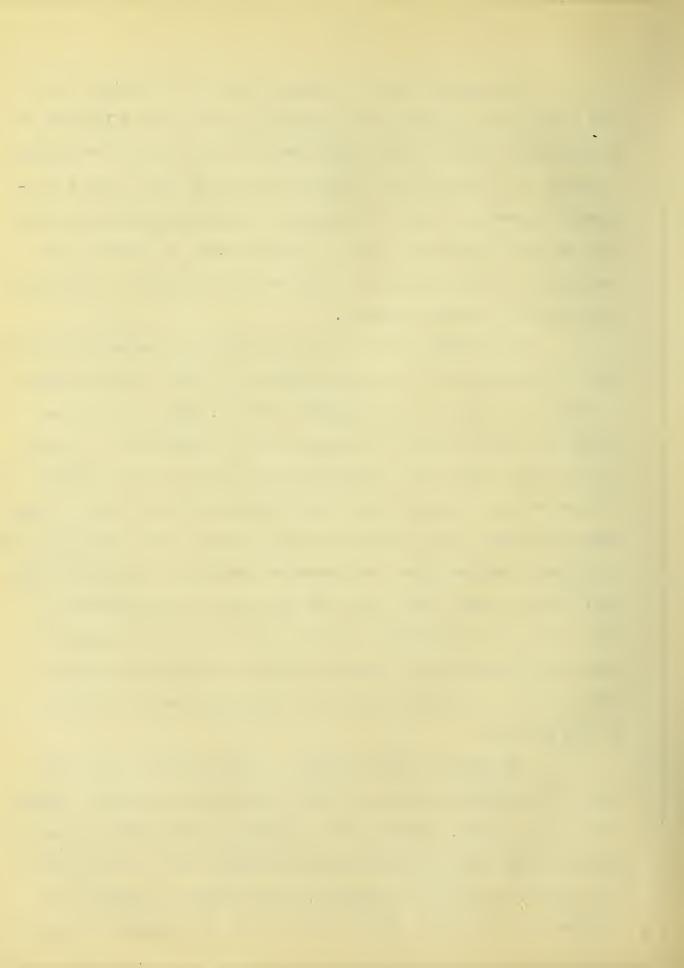
The stockholders of companies organized under this act are also made liable jointly and severally to servants and apprentices for all debts due and owing, only, however, after an action. The directors are also made liable for any loss due to dividends made when the company is insolvent.



The general act of 1852 providing for building boats and transporting persons and property thereon, not only made the stockholders liable to the creditors for all sums due on account of stock or otherwise, but specified how such sums might be recovered; namely, by suit in chancery, or by proceedings against them as garnishees; and provided further that no transfer on assignment of stock should be made so as to change or affect any liability at the date thereof.

ance of liability by the mere transfer of stock. In Florsheim v. Illinois Trust and Saving Bank, 192 Ill. 382, the supreme court held that the mere assignment by a stockholder of a part of his stock before the institution of a suit by the receiver of a corporation to collect the unpaid balance of the stock, to pay corporate debts, does not relieve the assignor from liability for the unpaid balance upon the shares so assigned. But in 102 Ill. App. 507, the court held that when the stock is transferred in good faith to a responsible person and not for the purpose of escaping liability such transfer has the effect to release the liability of the person making the assignment and to transfer it to the assignee.

The general railway act of 1872 imposed a liability upon stockholders similar to that imposed by the general corporation act of 1872, namely, to an amount not exceeding the amount unpaid on the stock; and no person holding stock in any corporation under this act as executor, administrator, guardian or trustee, and no person holding such stock as callateral security



is held personally subject to any liability as stockholder; but the person pledging this stock is considered as holding the same and is liable as a stockholder accordingly.

Thus we see that the liability of stockholders in railway companies has been of varying degrees undergoing an evolution from the unlimited to the limited.



Liability of Members of Insurance Companies.

It was not until the century was far advanced that any insurance companies at all were organized in the state. In 1835 the Alton Marine and Fire Insurance Company was organized and incorporated. It was provided that in any case of loss or losses whereby the capital stock of the company should be lessened before all the installments were paid in, each proprietor's or stockholder's estate should be held, accountable for the installments remaining unpaid on his share or shares at the time such loss or losses took place; and the company was prohibited from making any subsequent dividend until the profits of the company were such as to restore such losses to the capital stock. Thus it will be seen that the liability of stockholders in Marine and fire insurance companies is limited to the amount of unpaid stock from the very first.

However, it must not be thought that the provisions respecting the liabilities of stockholders and insurance company are all as simple as the one just cited. The charter of the Illinois Mutual Fire Insurance company (Feb. 23, 1839), after providing that every member of the company should be bound to pay his proportion of the losses and expenses happening or occuring in or to said company, goes on to say that "all buildings insured by and with said company, together with the right, title, and interest of the assured with the land on which they stand, shall be pledged to said company; and the said company shall



have a lien thereon against the insured, during the continuance of his, her, or their policy." Thile all buildings insured by the company, together with the title of the land on which they stand are thus pledged to the company for the payment of losses, it does not follow that the stockholders are liable to the full extent of such property, but only in such amount as may be due the company, for the act specifically places a limit on such liability. In case it should happen that the whole amount of deposit notes, which the members of the companies are required to make, should be insufficient to pay the losses occasioned by a fire, the sufferers are to receive toward making good their losses only a proportionate divident of the whole amount of said notes, according to the sums by them respectively insured, and, in addition, a sum to be assessed to all members of said company not exceeding fifty cents on every one hundred dollars by them insured. It must be seen that the company is thus provided with an automatic device for keeping its assets and liabilities on a par with each other except in case all buildings insured in the company should be destroyed at the same time, an inconceivable supposition.

In a number of companies organized during this period it is provided that in case any loss or losses took place equal to the amount of capital stock and the president and directors, after knowing of such loss or losses should subscribe to any policy of insurance, their estates jointly and severally, should be accountable for any and every loss taking place under policies so subscribed.



The Logislature of (1857) provided in the charter of the Union Insurance and Trust Company that the real and personal property of each individual stockholder should be liable for any or all losses and liabilities of the companies to the amount of the stock subscribed or held by him and not actually paid in; but with the additional stipulation that in all cases of losses exceeding the means of the corporation, such liabilities were to be paid, pro rata, by each stockholder, according to the amount of unpaid stock held by him.

Practically all of the insurance companies provide that persons entering for insurance must deposit with the Secretary of the company their promisory note payable in part or in whole at any time when the directors deem the same requisite for the payment of losses by fire, or for such incidental expenses as may be necessary for transacting the business of the company. The amount of such notes aften varies. We find the legislature of 1857 giving the Peoria Mutual Fire Insurance Company permission to require on such promissory notes a sum equal to one and one-half per cent on the amount of property insured; and for the purpose of raising a contingent fund for the payment of losses and other objects of the company, the company was authorized to exact of its members interest at a rate not exceeding six per cent per annum on the amount of said promisory notes, as long as the directors thought the company required it.

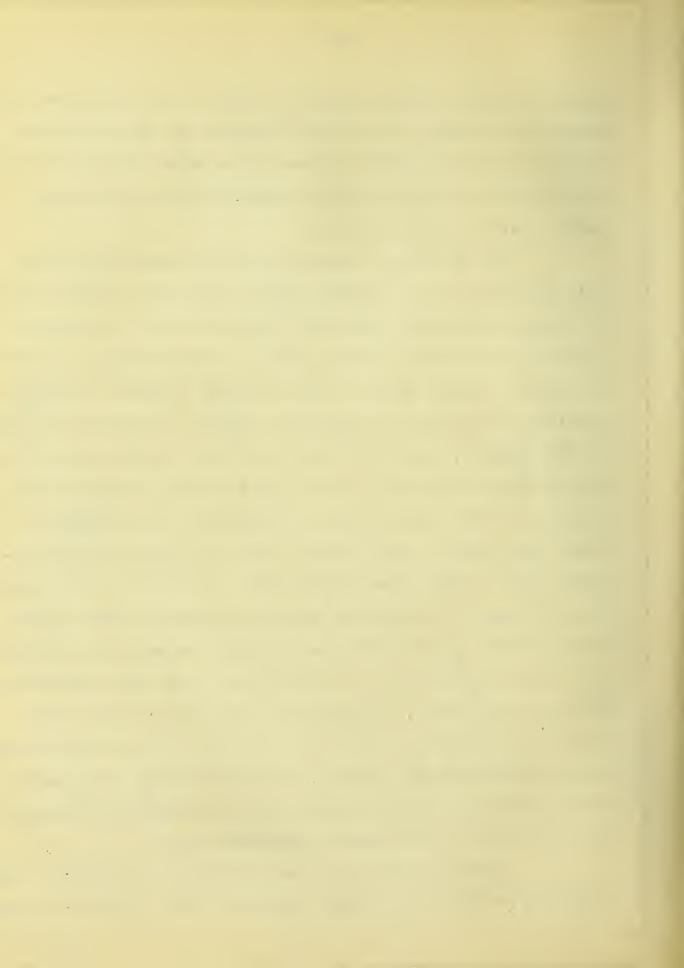
The **l**egislature of 1857 in incorporating the Joliet Insurance Company very wisely provided that while the capital stock paid in, and real and personal property of the company



should be liable for the payment of taxes in the city where the company was located, it expressly relieved the stockholders of liability for the payment of taxes on the same stock held by them which had been assessed to the company. This of course, was meant to avoid double taxation.

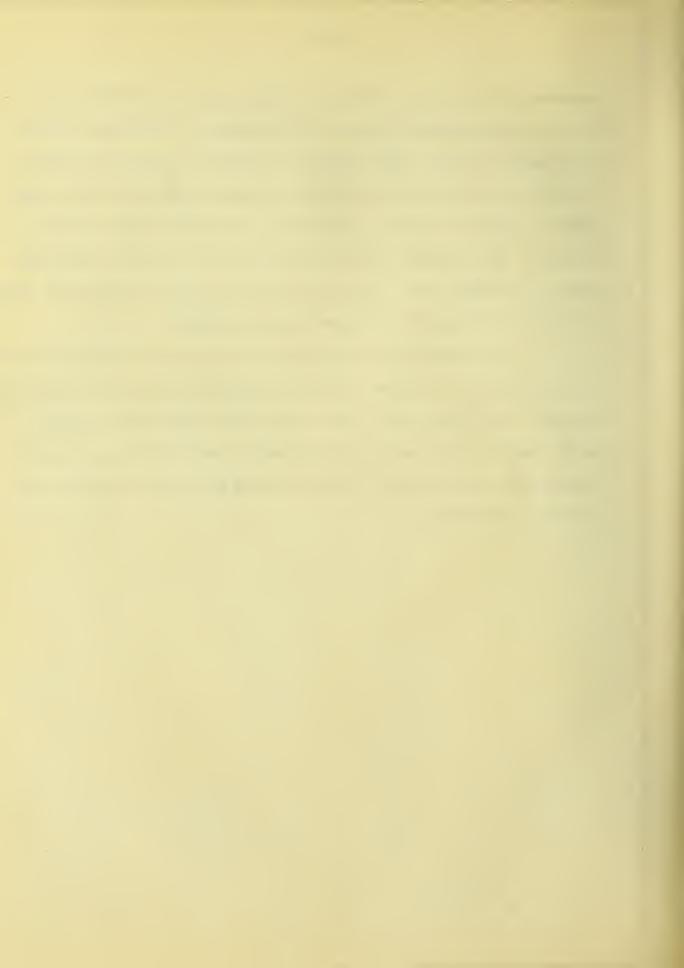
All of the acts incorporating insurance companies of this period are very implicit, sometimes detailed in their effort to fix and secure the liability of stockholders. A section of a charter of the Crete Farmers Mutual Insurance Company of 1861 is typical: "Every member of said company is bound to pay his portion of all losses and expenses happening or occuring in and to said company, during the time that he is a member thereof; and all buildings insured by and with said company, together with the right, title and interest of the assured to the lands on which they stand or are situated, shall be pledged to said company; and the said company shall have a lien thereon, for securing the payment of such sums as may be assessed on the deposit notes for the purpose authorized by this charter; and such lands or so much thereof as may be sufficient to pay such assessments on the deposit notes, together with the costs of suits, maybe sold on any execution isued out of a court of record, underjudgment recovered by said company, or account of the non-payment of such assessment, any law exempting home-steads from execution or any other law to the contrary notwithstanding."

In cases where, on account of the paid up nature of the stock the members are not held liable for debts, it then becomes



necessary to hold the officers of the company strictly accountable for unnecessary losses. For instance, the charter of the Northwestern Mutual Life Insurance Company, incorporated Feb. 18, 1865, provides that no member, except officers of the company and agents thereof, should be personally liable for the losses of the company; and such officers and agents severally were to be held liable, but only for the losses arising by reason of their own respective neglect or misconduct.

In conclusion we may say that insurance companies have always imposed a limited liability upon their members. In this respect they differ from other companies which often in the early years of the century held their stockholders personally responsible for debts to the full extent of their respective private capacities.



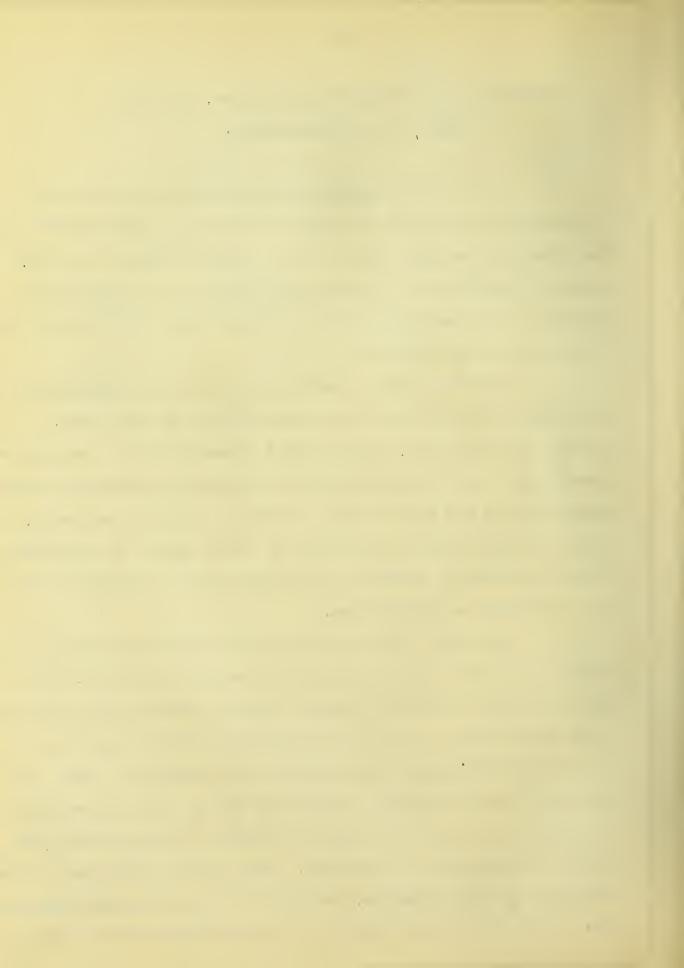
Liabilities of Stockholders in Banks, Loan and Joint Stock Associations.

In 1835 the General Assembly incorporated the subscribers to the Bank of the State of Illinois, and provided that the stock in the bank should in all cases be subject to a lien in favor of the bank for all debts bona fide due, or then owing. When the stock was fully paid up it would seem as if we have here a case of double liability.

By 1848 banks had become of sufficient importance to call forth a section in the new constitution of that year.

Article X, Section IV, privides that "stockholders in every corporation or joint stock association for banking purposes issuing bank notes or any kind of paper credit to circulate as money, shall be individually responsible to their amount of respective share or shares of stock in such corporation or association for all its debts and liabilities."

The years 1849 to 1851 inclusive saw the passage of a number of general incorporating acts, as has been noted. In 1851 the General Assembly passed a general banking law providing that stockholders in companies organized under its provisions should be individually responsible to the amounts of their respective share or shares of stock for all of its indebtedness and liabilities of every kind, to the full intent provided for in the constitution of the state. This act was submitted to the governor for his signature, but met with his strenuous disapproval. In fact he vetoed the bill, giving as his reasons that the



bill nowhere provided a safe adequate personal liability of the stockholders for the redemption of the notes they have caused to be put in circulation. The bill, he maintained, actually provided against the liabilities of the stockholders except to the extent of the security required to be deposited with the auditor and the value of the shares in the bank, which might be worth something or nothing, according to circumstances. He thought the stockholders should be individually liable "If it be the design to have banks conducted honestly", - he avers, "and the interest of the state protected against fraud, the stockholders have not just ground of complaint, at this precautionary requirement; but if not, the bill holder has no greater security than he is entitled to, to protect himself against losses and dishonesty." He thought that if there were a thorough going personal liability for all the bank's liabilities, it would supply what has long been needed in conducting the affairs of banks. It would bring that keen sense of direct personal interest, among the strongest of all safe guards, to hear upon the direction and general management of all banking institutions. But despite the governor's objection and veto the General Assembly passed the bill over his head. That the governor was right in desiring a more adequate liability, history has undoubtedly proved.

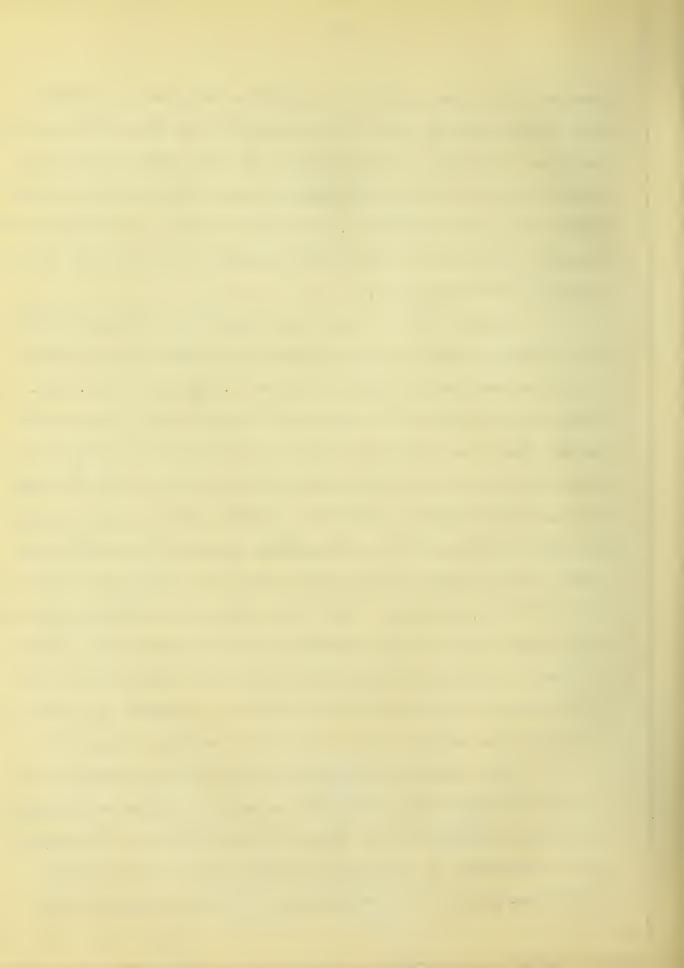
The law not only provided for the liability contemplated above, but it made such stockholder's liability to continue for a space of six months after the assignment by him of any such stock; and added that any stockholder who is really the



partner in interest, should be liable as aforesaid, although such stock might be held and recovered in the name of some other party or individual. The intention of this latter clause was doubtless to hold both the transferor and the transferee liable within the period mentioned, although of course, a creditor according to law could proceed only against but one of the two according to circumstances.

Exactly what is meant by making a stockholder liable for a period after he has transfered his stock was determined by the supreme court (1877) in Fuller v. Ledden 87 Ill. 310. In this case the charter of a bank had provided that each stockholder should be liable to double the amount of stock held or owned by him and for three months after giving notice of transfer. The court held that a creditors right of action is not limited to three months after the stockholder sells and transfers his stock, "since such provision has reference to the continuence of the liability, and not to the time within which action shall be instituted; and the fair construction to be given the language is that the stockholder shall be liable for such debts as are contracted by the corporation while he is a member and during the ensuing three months after he has given notice of transfer."

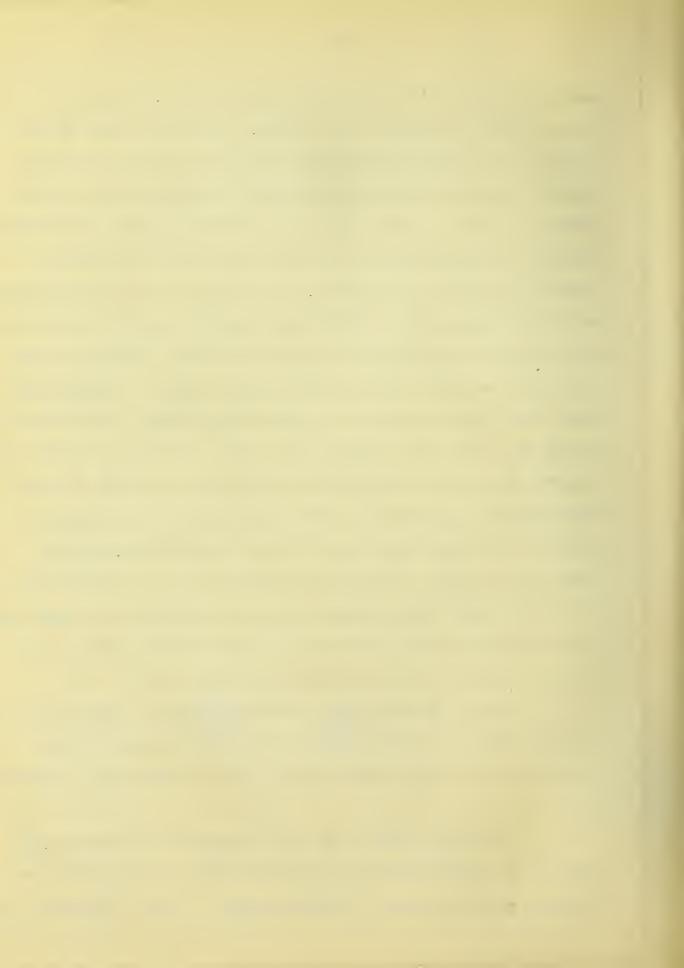
The general act further provided for proceedings in liquidation when the assets were exhausted. After authorizing any person having right or cause of action upon or on account of any indebtedness or liability to bring suit in any court of record having jurisdiction against the stockholders for the



amount due upon such indebtedness or liability, it goes on to say that in order to enforce this remedy, "any such person may institute and maintain any appropriate action or suit in equity against the corporation or association and upon trial of such action or hearing of such sait, if judgment or decree is attained against the corporation, the court shall direct an issue or issues to be made in the cause, for the purpose of ascertaining and deciding upon the liability and extent thereof of each stockholder under and according to provision herein and of the constitution; and upon the decision of such issue or issues the court shall enter judgment or decree against each stockholder for the amount and to the extent of his, her, or their liability so ascertained; upon which judgment executions may issue against the stockholders in succession, until the amount of the judgment against the corporation shall be paid or collected, or the liabilities of the stockholders extinguished; and payments or collections made upon judgments against stockholders, shall operate to extinguish the liabilities of such stockholders to the extent or amount of such payments or collections."

In the charter of the Farmers' Savings, Loan and Trust. Company (1857) we find the stockholders held liable to their creditors only to the amount of the capital stock each has paid in.

From this time on we find a growing tendency on the part of the legislature to be a little more exacting with reference to the liability of stockholders in banks, buildings and



loan associations. The charter of the Alton Building and Savings Institution (1857) not only provided that stockholders of the company should be severally individually liable to the depositors with and creditors of the country to an amount equal to the amount of the stock held by them, respectively, for all the deposits made with and debts and contracts made by the company, but provided in addition that such personal liability should continue for the time of two years from the sale or transfer of such stock by any stockholder. However, the stockholders were relieved of personal liability for the payment of deposits made with or debts contracted by the company unless a suit for the collection of such deposit or debt were brought against the company within one year from the time the same became due.

A case involving this kind of liability was decided by the supreme court in Schalucky v. Field. 124 III. 617. The court held that the officers of a bank in making written entries of the deposits in pass books of the depositors, act as the agents and representatives, not only of the corporate entity, but also of the stockholders, regarded as un-incorporated partners; and such entries are as binding on them as upon the bank, in a suit by a depositor to enforce their individual liability. In 117 III. 619, the court held that where the charter of a banking corporation makes its stockholders individually liable to the amount of the stock held by them, respectively, to the depositors and and other creditors of the bank, for any losses that they may sustain, such liability is a common fund for the security of



covery, will have jurisdiction of a bill by a creditor, for himself and others, to enforce such liabilities, and control the fund thus raised for their benefit, and distribute the same ratably among them, the remedy at law in such case being inadequate with out the bringing of a multiplicity of suits. "Undoubtedly" says the court, "the law is, where a common fund exists upon which numerous persons have claims, equity will seize hold of, and pay it out ratably upon their respective claims, or pay them in full, if the fund shall be sufficient for that purpose in cases where it is wrongfully with held."

While a number of the acts of this period continues to hold the stockholders in banks and trust companies liable only to the amount of their stock as provided in the constitution, yet the tendency toward stricter liability was becoming all the time more noticable, culminating in the heavy liability of the general banking act of February 20th, 1861. This was entitled "An act to establish a General System of Banking upon a Specie Basis in the State of Illinois." The stockholders of every branch of the bank are "held and bound to an amount over and above their stock, equal to their respective shares for all the debts of said bank or any of her branches." They were also liable for a period of six months after the transfer of their stock. A great many of the charters during the sixties provided not only for double liability but also that no assignment of stock should release the stockholders from their liability until after the fact of



such assignment and the name of the person to whom made, and the amount of the said stock, had been advertised in some public newspaper for a period of three months. Out of a total of sixty seven banks incorporated in 1869, eight only provide for double liability; the rest, to the amount of capital stock held by the stockholder.

To sum up we may say that not a single case of unlimited liability has been found in the case of banks, loan and saving institutions. In the case of manufacturing and general business companies, especially during the first half of the century we found many cases of unlimited liability; and one would think that if the principle of unlimited personal liability is applicable and justifiable any where, it would be in the case of banks and trust companies, on account of the peculiar nature of such companies, being as they are the depositorics of savings and profits of innocent citizens; but such has not been the case. The stockholders of banking associations and trust companies in general have been from the very first responsible only to the amount of their stock, and not until during the sixties to double the amount of their stock.

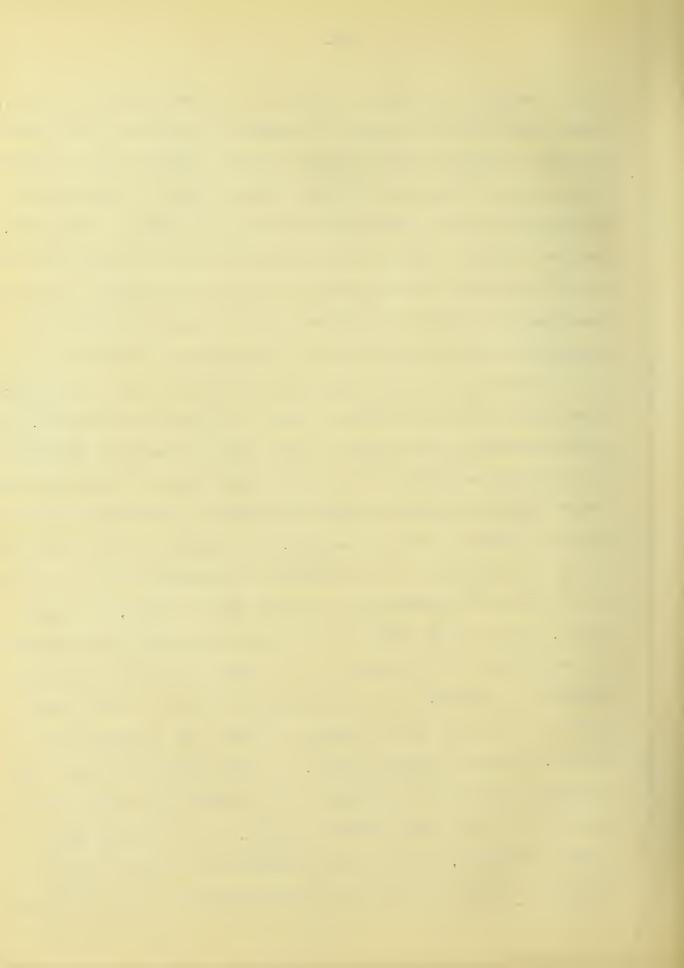
\*\*General Recapt Questions\*\*

There are a number of general legal questions respecting the liability of stockholders, their rights and duties, the
transfer of stock, fraudulent over valuation, receivership, etc,
which it may be well to consider here.

When stock is transferred, who is liable on it, the assignor or assignee? In 110 Ill. 316, the Supreme Court lays down the general principle that "there can be but one amount for

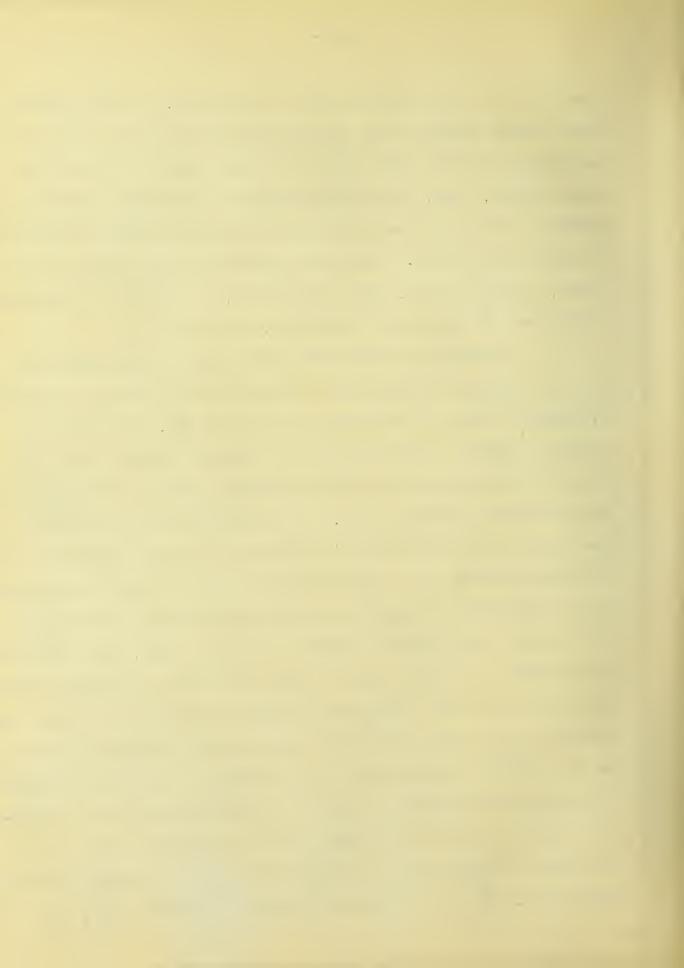
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which there is liability on account of the same share of stock, where that liability equals or exceeds the amount of such share. For that amount both the assignor and the assignee may be liable, the assignor because the debt was incurred by the corporation within three months after the date the assignment of the stock, and the assignce because it was incurred after he became the holder of the stock; but there can be but one satisfaction. It has been decided, where the assignor is held liable on account of such stock after he has sold and transferred it to another, that he is entitled to recover the amount from the holder into whosever hands it may have passed, upon the ground as expressed, that each successive owner stands in his shoes as respects the stocks and liabilities growing out of it: These cases," continues the court, "proceed upon the hypothesis that the stock has attached to it a liability equal in amount, on account of debts incurred by the corporation, to be discharged by whomsoever is, at the time such debts are incurred and for three months after, its legal owner, and not upon that of the successive personal liabilities of each holder to the amount of the stock for debts contracted while he is holder. If each successive holder of stock maybe charged with debts to the amount of stock, as a personal liability, because of being holder, it would seem quite plain the assignee ought not to be liable to re-emburse his assignor on account of a liability incurred by him, for in that event a double liability, might in many instances be imposed on the assignee. If the liability is purely personal, then the person



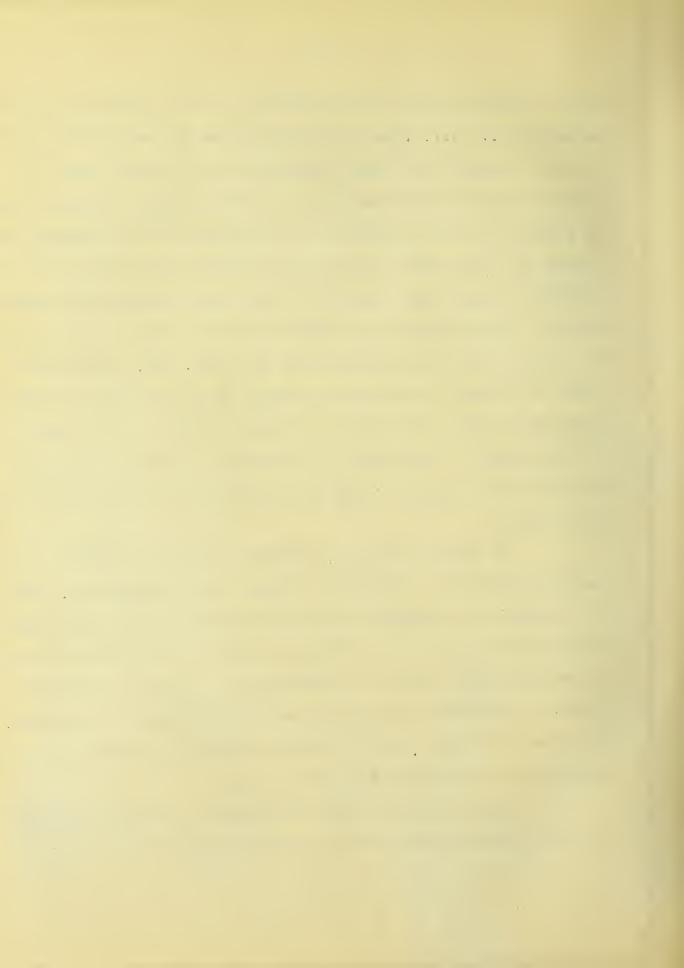
upon whom it is east should bear it, moreover, if each successive owner simply stands in the shoes of the first owner, and is only required to do what that owner would have had to do had be remained owner, then, since one payment of a liability equal to the amount of the stock, would have relieved him of future liability, it must relieve them. The burden attaches to and goes with the stock, as an incident, until discharged, and should be discharged by him who, at the time it attaches, is owner."

A number of complicated cases have arisen respecting the liability of stockholders in foreign corporations. In Tuttle v. National Bank of the Republic 116, Ill. 497, the court was asked to enforce liability under the Kansas Constitution. In this particular case the right to recover rested on the statute of the State of Kansas alone, as the constitutional provision was not self enforcible and the liability was only attempted to be made resultant from legislation providing a special remedy and by the construction placed on that legislation by the courts of that state. The Illinois Supreme Court held that, "the statutes of the State of Kansas have no force and effect in another state, and the enforcement of a remedy in this action in this state, depends upon our expressed tacit assent, which is usually expressed as the comity between states. The extent to which this principle of comity may proceed is subject to qualifications and restrictions which in almost all cases, are to be determined by the particular sovereignty. A remedy special to a particular foreign state is not by any principle of comity enforcible here, and



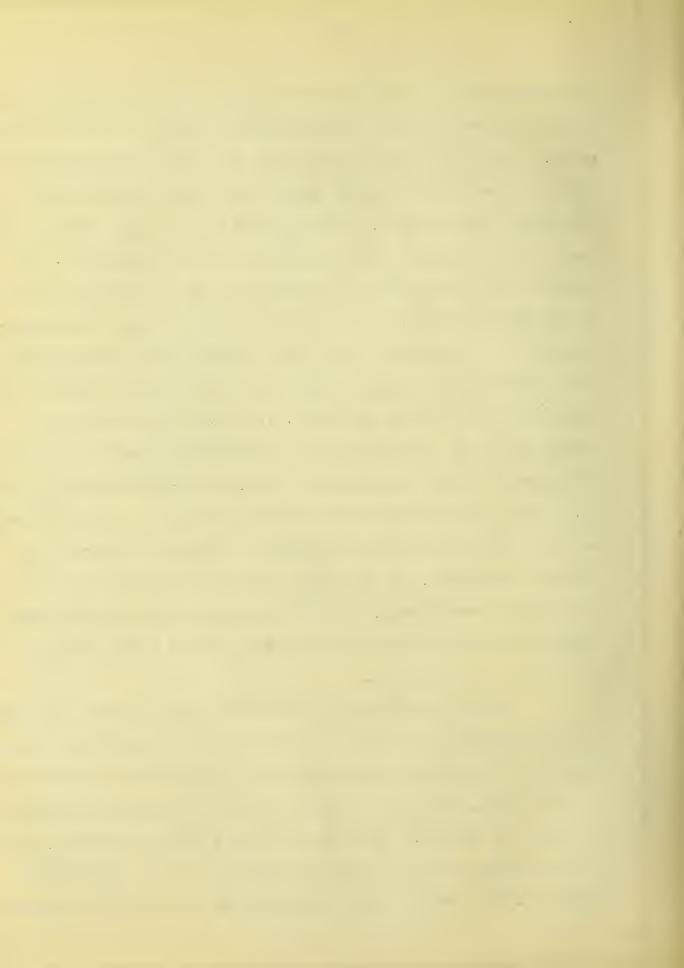
Of course, where no statutory remedy is provided the sase is different. Elliott on Private Corporations says, "When the legislation creating a corporation declares that the stock-holder therein shall be individually liable for the debts of the corporation under certain circumstances but fails to provide a method of proceeduire by which the liability shall be enforced, it is generally held that it can be enforced in another state, according to the proceedure of the forum."

An interesting case arises where a stockholder of an insolvent corporation is also a creditor to the corporation on



his subscription, or for property of the corporation unlawfully paid to him as by way of unauthorized dividends or on any other cause. "The proper thing for him to do", says Clark on corporations, citing Illinois cases among others to substain himself, "is to pay what he owes, and then come in and share ratably with the other creditors in all the assets of the corporation. He can not, when sued upon his indebtedness by or for the benefit of all the creditors, set off the debt due him from the corporation, for to allow this would be to permit him to appropriate this asset of the company to the payment of his own claim to the exclusion of the other creditors......If it is sought to compel them each to contribute a proportionate sum to a fund for the payment of all creditors pro rata, a set-off can not be allowed. Where, however, an action is brought by a single creditor, as may be done under some statutes, to enforce a several and original liability, for the sole benefit of the company suing, it is held, anomalously, by the weight of authority, that upon equitable grounds the stockholder may set off a debt owing to him from the corporation.

One of the most perplexing situations arises where the statute provides no remedy for enforcing the liability of stock-holders. It is here that we find much confusion and conflict in the decisions. The perplexing question is whether the remedy is at law or in equity. Shall the suit be brought on behalf of all the creditors or by one creditor against a single stockholder? Naturally this depends upon the nature of the liability created,



and one must give particular attention therefore to the wording of the statute. "By the weight of authority" says Clark on Corporations, "if the object of the statute is to provide a fund out of which all the creditors are to be paid, share and share alike, and to make the stockholders contribute to it in proportion to their stock, remedy is by general creditors bill, or suit of that nature, in which an account may be taken of the debts and stock and a pro rata distribution be made among the several stockholders, and the fund thus obtained may be paid pro rata to all the creditors, and, under such a statute, an action at law by a single creditor against a single stockholder will not lie." (Quenan v. Paler 117, Ill. 619). But, if, on the other hand, the statute makes each stockholder severally liable directly to the creditors, and fixes the liability, making it independent of the liabilities of other stockholders so that there is no necessity of involving other stockholders or creditors, in that case any creditor after recovering judgment, may maintain an action against a single stockholder. In other words "where the liabilities of the stockholders is several and an action at law is brought, each must be sued separately." (Fuller v. Ledden 87, Ill. 310; Schalucky v. Field, 124 Ill. 617). This same point was sustained (1885) in Rounds v. McCormick, 114 Ill. 252. Here it was held that an action at law by a creditor to enforce the liability of a stockholder in a corporation organized under the act of 1857 entitled "an act for the formation of manufacturing, mechanical and chemical corporations", will not lie, since the liability of the stockholders in such a corporation is to the creditors as a

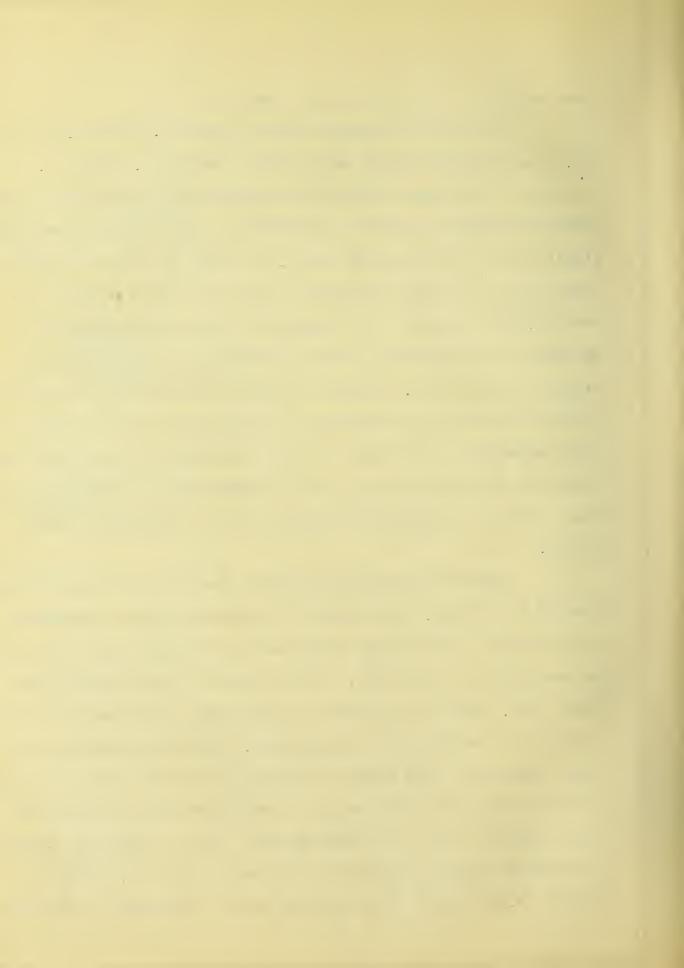


class and not to each individual creditor.

In 1889 the supreme court in Dupee v. Swigart, 127 Ill.

494, declared the banking act of 1887, section 6, clause 1, in
so far as it provides that a claim against the bank must be proportioned ratably among the stockholders, each stockholder being
liable only for his ratable share, and that the owner of such
claim was to sue each stockholder for the latter's ratable proand
portion, that a share of an insolvent stockholder can not be
collected of the others, is void as in conflict with the constitution article X1, section 6, which provides that every stockholder in a banking corporation or institution shall be individually responsible and liable to its creditors, over and above the
amount of stock by him held, to an amount equal to his respective
share, for all liabilities accruing while he remains a stockholder.

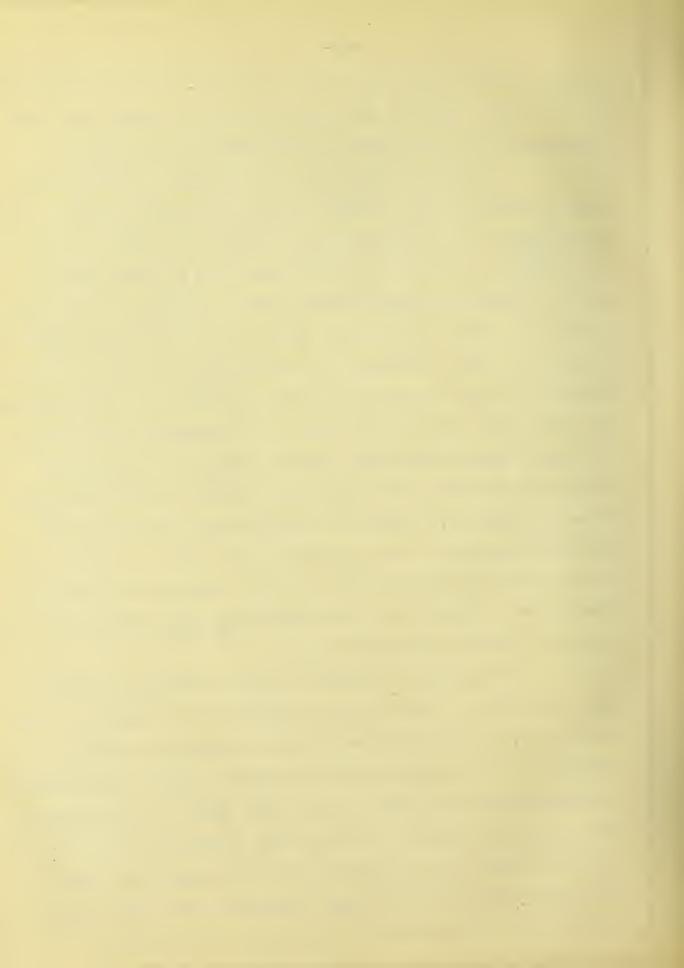
Another interesting question decided by the courts is that of the status, and relation to stockholders and creditors of the reciever. The supreme court was called upon in 98 Ill. 135, to determine this question. In the course of its opinion the court said, "when the receiver is appointed, he succeeds to the right of the bank in all its property, claims and demands, to sell, dispose of, and reduce to money to be paid under the order of the court to the creditors of the corporation according to their rights. He, by his appointment, does not become a trustee or guardian for the depositors, to manage, control, settle or enforce their individual claims by suit or otherwise. The statute



having conforred the right on the depositor, it is as absolutely his individual claim as any claim he may hold against any other individual for or on account of any business transaction."

In this same case the court decided a point which we have discussed in part before. We have seen that whether a stockholder may be sued separately by a creditor or whether he is to be proceeded against by a general creditors bill and thus be made to contribute ratably depends upon the nature of the statute. In 87, Ill. 310, and 124, Ill. 617, the court held that where the liability of the stockholder is several, and an action at law is brought each must be sued separately. In the case under discussion the court suggests a remedy for a stockholder who has been sued and judgment recovered against him upon his individual liability as fixed by the statute. "He is no doubt", to quote from the decision, "entitled to contribution from all of the other shareholders, and in enforcing that right, it may be in such a case equity would be the proper forum, as he could thus compel each shareholder to contribute pro rata, according to the number of shares each might hold."

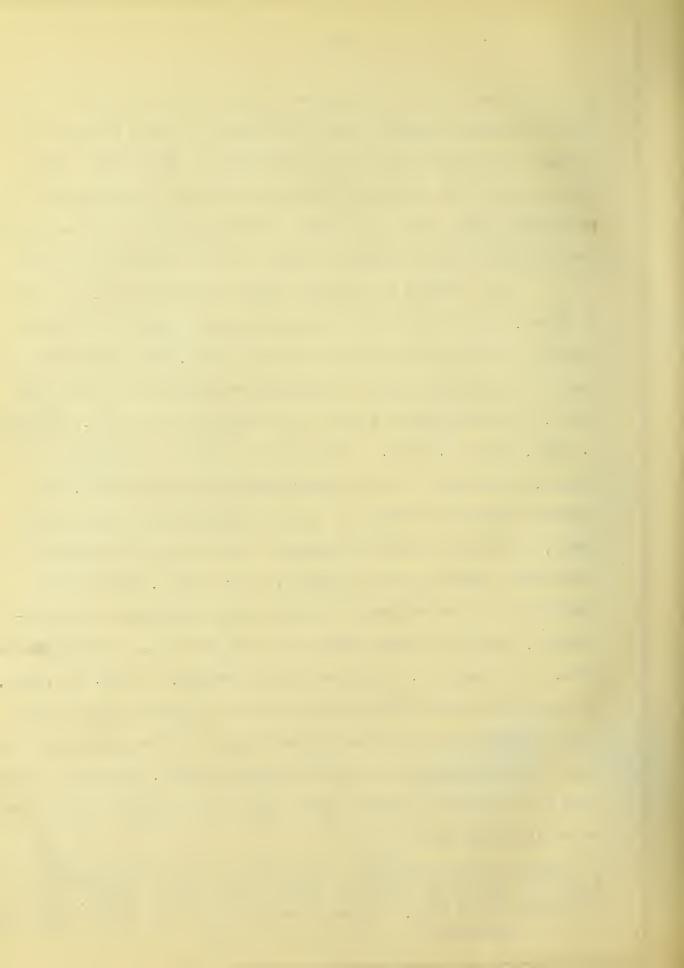
The gradual evolution of the principle of liability has been noted. Now if the statutes hold stockholders liable on the unpaid portion of their stock and credit is given to the corporation on the theory that the capital stock of the company represents money or money's value there ought to be no loophole for escaping liability. If in theory stockholders are liable on their stock, and in practice they claim that thier stock has been given to them and that consequently they owe nothing on it, or if the capital of the company has been used



up in dividends, or if they have received their stock in return for over-valued property and thus manage to avoid responsibility, of what value after all is the principle of liability? What guarantee has the creditor that the statutory liability will be enforced by the courts under all circumstances? What has been the attitude of the Illinois courts on this important matter?

The courts of Illinois have uniformly held, so far as is known, that unless there was entire good faith in valuing property taken by the corporation for stock, the stockholder must respond to creditors of an insolvent corporation for the par value, less the actual value of the property so taken. (Coleman v. Howe, 154 Ill. 458). In 1892 the Appelate court held that "Where, previous to the incorporation of a partnership, the partners agreed to convey to the corporation partnership property, receiving therefor corporate stock double the amount of the actual value of such property, they cannot, as against creditors in proceedings to enforce their liability as stockholders, claim that such stock is fully paid up, and non-assessable." In Thayer v. El Plomo Mining Company, 40 Ill. App. 544, the court held that "stockholders of an insolvent corporation will be liable to creditors unless there has been given for the stock the equivalent in money or money's worth. On this question then the courts of Illinois have been very explicit. be no loophole here.

<sup>1.</sup> Public policy forbids a corporation to create as against its creditors stock for which it has not received in property or money its full face value as represented by the shares. Elliott on Corporations says, "Persons who purchase such shares from the (continued on bottom of next page)



Another phase of this problem is that of liability on bonus stock. Some times a corporation gives away stock in order to reduce its nominal percentage of profits, or as an inducement to subscribers to take some of their other stock or bonds. In 1892 the supreme court of Illinois was called upon to decide a case involving this principle. A company, organized to build a dam for manufacturing purposes, had obtained a donation from a city in bonds to be applied in building the dam. The company thereafter issued stock to the several original subscribers in amounts equal to the amount of the bonds donated by the city, for which the subscribers paid nothing. The court held, on a judgment creditors bill, that the stock so received by the subscribers, should be subjected to the payment of the debts incurred by the corporation in erecting the dam.

while the Illinois courts have thus uniformly held stockholders liable for corporate debts on bonus stock or on stock received in exchange for over-valued property, nevertheless they have regarded such transactions as binding on the corporation as between itself and its stockholders. In 208 Ill. 544, the court held that fraudulent overvaluation of property turned over to a corporation by stockholders in payment of their subscriptions, while it renders the transaction voidable as to creditors

corporation at less than their par value are, in the event of insolvency of the corporation, liable to pay for the benefit of its creditors at least the difference between that which they have actually paid and the par value of the shares. The issuance of the shares is treated as a representation to the public that the corporation has property equivalent to their face value." Hawley v. Upton, 102 U. S. 314; Scovill v. Thayer, 105 U. S. 143.



and other stockholders prejudiced thereby, is binding upon the corporation, and as between the corporation and stockholders the stock subscription is fully paid."

It is thus evident that the corporation can not assess such stock; and the only case in which such stockholders can be called upon to contribute the difference between the nominal. value and the actual value of their stock, is after the corporation has become insolvent and unable to pay its debts.

It has been held that a stockholder who has received dividends paid out of the company's capital stock, although he received them in good faith and ignorant of their source, may be held liable for such capital so received by him. Equity will require him to contribute pro rata for the payment of the company's debts. "The stockholders have no rights to anything but the residuum of the capital stocks, after the payment of all the debts of the corporation. If before all such debts are discharged, they take into their hands any of the funds of the corporation, they hold them subject to an equity which it is against conscience to resist." (Clapp v. Peterson, 104 Ill. 26). This is believed to be the attitude of the Illinois courts. However, the supreme court of the United States recently held that the receiver of a national bank can not recover a dividend paid entirely out of capital which the stockholder received in good faith, believing the same to be paid out of profits, and the bank at the time he received the dividend was solvent. "We think the theory of a trust fund has no application to a case of this kind. When a corporation is solvent, the theory that



its capital is a trust fund upon which there is any lien for the payment of its debts has in fact very little foundation. No general creditor has any lien upon the fund under such circumstances, and the right of the corporation to deal with its property is absolute so long as it does not violate its charter or the law applicable to such corporation." McDonald v. Williams, 174, U. S. 397. It seems to be the settled opinion of the United States supreme court that the property of a corporation is a "trust fund" only after the corporation becomes insolvent. This, however, as noted above is contrary to the ruling of the Illinois courts and contrary to the accepted doctrine of many other state courts.





